D̶S̶-SX-PF

Lloyds Bank Review

1677

OCTOBER 1949

Lloyds Bank Limited

Head Office: 71 LOMBARD STREET, LONDON, E.C.3

Lloyds Bank Review

New Series | OCTOBER, 1949 | No. 14

TABLE OF CONTENTS

The Bank publishes from time to time in this REVIEW *signed articles by exponents of different theories on questions of public interest. The Bank is not necessarily in agreement with the views expressed in these articles. They are published in order to stimulate free discussion and full inquiry.*

The Sterling Problem

By Lionel Robbins

IT takes a lot to upset us nowadays. But the recent worsening of our balance of payments and the drastic devaluation of the pound have caused widespread bewilderment and anxiety. We were aware in a vague way that the position was not yet sound, that there was much to do before Marshall Aid came finally to an end in 1952. But the improvement last year, as compared with the disasters of 1947, had tended to conceal the essentially precarious nature of the contemporary position; and the fact that in 1949, with Marshall Aid still in full blast, our reserves should be dwindling at a rate which, if continued, would involve substantial cuts in consumption and widespread unemployment, has come as a severe disappointment. It is improbable that the great mass of the people yet realize at all the nature of the peril which threatens them: it is the nature of the system under which we live that it tends to insulate the man in the street from the premonitory symptoms of danger. But it is safe to say that the majority of informed opinion is now thoroughly disquieted. The fact that, for a second time, we have run into acute difficulties, while actually in receipt of massive aid from abroad, must surely suggest to serious minds in all parties that, however much we may have been the victims of bad luck, the implications of our own policies are in urgent need of re-examination.

It is in the hope of contributing to this process that the following notes have been written.

I. False Scents.

Let us first try to clear our minds of false scents and inadequate explanations.

(*a*) *The American Recession.*

There can be little doubt that one of the chief factors contributing to the recent decline of our reserves was the falling off of demand for colonial products, due to the cessation

of inflation in America. It is not yet possible to give a quantitative assessment of this. But, when the figures are published, it will be very surprising if the decline in price of such commodities as cocoa and rubber does not stand revealed as one of the most significant single causes of our immediate embarrassments.

It is one thing to recognize this influence, however; it is quite another to jump to the conclusion that it is the only influence that we need take into account, still more that the whole blame for our present difficulties can be placed on American shoulders. For, in the first place, it is not the only influence. Quite apart from the decline in confidence which has been the by-product of rumours of trouble, it is unfortunately a fact that the volume of exports from this country has fallen and that the selling of our goods abroad is encountering rapidly growing difficulties. Not only in the dollar area, but in other quarters, the sellers' market tends to come to an end. The days when the inadequacy of our exports could be ascribed to difficulties of production rather than difficulties of sale are over. And, despite all that has been done, we are still far short of the wished-for goal.

It is, therefore, to get things quite out of proportion to regard the fluctuations of American demand as the sole occasion of our difficulties. It is even more mistaken to suggest that there is anything which reflects any special blame on the conduct of American policy in the extent to which these fluctuations have actually affected us. For what has happened so far in the United States cannot by any legitimate stretch of the meaning of words be regarded as a depression. There has been a cessation of inflation and a readjustment of certain prices—greatly to the benefit of American consumers. There has been a small falling off in the volume of production as compared with last year and some lag in the absorption of new recruits to the labour force. But there is still high prosperity in the United States; in all probability 1949 will be recorded as the second best year in American economic history. Whatever may be coming later on—and I make no prediction in these matters—it is just a sign of ignorance to regard what has happened so far as anything but a very minor recession. If our arrangements are so fragile that they cannot stand up to that without our whole future being jeopardized, then there is something very wrong with our arrangements: we are

altogether too good to live. The member of parliament who recently attributed all our trouble to the inability of Congress to manage the American economy was not merely guilty of extraordinary ingratitude and bad manners, he also showed a lack of easily accessible information and an absence of knowledge of the world which must suggest grave doubts of his own ability to manage anything at all.

(b) External Misfortune Generally.

For something of the same reason, it is not really very helpful to be always dwelling on our external misfortunes in general.

It is quite true that if we look around, it is not at all hard to compile a very respectable list of external circumstances whose absence would have been a material alleviation of the situation. Opinion may differ on the question whether before the War the general trend of trade was operating in our disfavour. But clearly there can be no question that our present difficulties owe their origin to the War and the dislocations and disturbances which have followed it. If our external assets had not been reduced, if we had not run into debt on an enormous scale, if the maintenance and increase of our capital equipment at home had not been sacrificed to developing the maximum striking power against the enemy, if we had not had to spend vast sums in policing various parts of the world, if other countries were in a position to pay us for what we sell in freely convertible currency, and if there had been no adverse turn in the terms of trade, how different the picture would be. It is possible to spend quite a long time attempting to assess the significance of these factors and dilating on their adverse effects.

But important as it is to know the nature of the misfortunes we encounter, it is no explanation of our present position just to list them and to leave it at that. For unless we are prepared to assume that the best possible policies are always automatically pursued, we must examine too the nature of the steps which have actually been taken to deal with these difficulties. We must ask whether they have been adequate to the occasion; we must even ask whether in some respects they may not have made things worse. When a ship encounters a storm, we do not immediately assume that it must be blown off its track. We ask what the captain has done. Has he shortened the right sails? Has he steered the vessel in the appropriate direction? We may

indeed conclude that the elements are too much for him, that having done all that was humanly possible, it is yet unavoidable that the voyage should be disturbed. But we do not take this for granted. Ships are not built, navigators are not trained, on the assumption that only calm weather is in prospect. So, in considering the fortunes of the ship of state, we make things altogether too easy if we are content to assume that the mere enumeration of external misfortunes is a sufficient explanation of deviations from the desired course. We all know that a great many adverse incidents have happened in the last ten years. The question is, have we done all that was within our power to meet them?

Now it is on just this point that it may be suggested that the burden of proof is with those who suggest that we could have done no more. For *prima facie* the contention is most unplausible. It is now four years since the end of the War. During this time we have received advances from abroad on a scale never before known in economic history. It cannot be said that there has been no time for adaptation; nor that there has been no assistance from elsewhere to ease the strain. Yet, when last we were given the figures, the adverse balance was running at a rate as great as the rate prevailing shortly after the War. No responsible person will wish to underestimate the very real difficulties which have made the transition period so much more arduous than at one time it was expected to be. But, in the face of these contrasts, it is surely hard to contend that there is not a case for enquiring whether in fact we have done all we could, or whether indeed some of the things which we have done have not proved to be additional aggravations of the position.

(c) *Nationalization.*

In making this enquiry, however, it is necessary to remember that the policies which are under examination are policies which, directly or indirectly, affect the balance of payments, the problem under discussion. We are not making a survey of policy as a whole. There may have been many acts of policy in the last four years with which we disagree and whose ultimate influence on the economy we think to be likely to be bad. But, unless in the period concerned, they have adversely affected the balance of payments, they are not relevant to the discussion.

For this reason, in what follows, there will be nothing said about recent acts of nationalization. I will confess frankly that I have no love for what has been done in this connection. I do indeed regard it as having ominous implications for our progress in the future. But I do not believe that, so far, it has greatly affected the balance of payments. I should not adopt this attitude to all possible nationalizations; in my judgement, the nationalization of steel or insurance would have very direct adverse effects that way. But I do not think that this can be said of most of what has happened up to date, the nationalization of the Bank of England, transport, coal, gas and electricity.[1] I can understand the argument that the frame of mind which has led Ministers to concentrate so much of their own energies and—what is quite as important—the energies of the high civil service on these somewhat doctrinaire manifestations of policy, to the neglect of the more pressing and immediate problems of domestic and external equilibrium, is symptomatic of much that has gone wrong in this critical period. I should not quarrel with this contention. But it is a different thing from the contention that nationalization itself has had so far any very direct influence on the vicissitudes of the balance of payments. It is policy in this respect that is the subject of the present enquiry.

II. Diagnosis.

(*a*) *The Export of Capital.*

If we start from the brute facts of the external accounts, the first item which is likely to suggest itself as a factor aggravating our difficulties, is the export of capital.

By this I mean either new investment or repayment of past debt. If we finance new construction abroad, if we extend the volume of short-term credits to overseas purchasers, if we allow existing sterling balances held in London to be run down, that is capital export; and, in present circumstances, that, directly or indirectly, is a strain on our resources additional to the strain of making payments for our own imports.

It is not very difficult to see how this happens. A direct strain arises if those to whom we lend or those who are claiming payment of sums left here in the past are allowed to turn their claims into gold or dollars. It should be clear that such operations must involve either a diminution of our own

[1] I should not wish to give so clean a bill to the abolition of the Liverpool Cotton Market.

reserves or recourse to borrowing in hard currency. We sacrifice financial resources without any contemporary return in the shape of imports. The expenditure of gold and dollars is unrequited by goods and services.

Much the same thing happens, although the process may appear to be more indirect, if the sums lent or repaid are spent on our own exports. If we export a larger volume of goods on credit or if the export of constructional equipment is paid for by drafts on sterling balances here, that means in effect that, to that extent, our export activities have reaped no equivalent entitlement to imports. The exports are unrequited by corresponding goods and services.

It is sometimes argued, with great parade of esoteric technical information, that this parallelism between unrequited gold and dollars and unrequited exports is invalidated by the fact that some exports are specific, so to speak, to particular markets while, of course, dollars can be spent anywhere. The cloths that we send, let us say, to certain parts of the East, the machines that we make for particular development projects, are not marketable elsewhere. To argue, therefore, that, if they are paid for out of new loans or old balances, that involves the sacrifice of an equivalent amount of current earnings is said to be illegitimate.

The argument has some superficial attractiveness. But in fact there is very little in it. The specificity of certain ranges of exports may be freely admitted—although it is important not to exaggerate it. It is quite true that in many lines of export, even if the goods are not actually bespoken, they are adapted in one way or another to the requirements of particular markets. But it is very rarely true that the labour, the machines, the raw materials which went to make them are so highly specialized as to be incapable of being put to any other use which, directly or indirectly, could swell the total of requited exports. The cotton goods which are sold in a special market may be incapable of sale elsewhere. But the burden of proof rests with those who argue that the cotton out of which they are made, the spindles which spin the thread, the looms which weave the cloth and the labour, which is concerned at different stages of manufacture, cannot be used for anything else. And let it be remembered that it is not merely direct use for other export markets which exhausts the possibilities. If the products which can be made from the resources originally

producing unrequited exports can serve at home as substitutes for other products made from resources which are capable of export production, the conclusion is the same : the unrequited exports involve a sacrifice of earning power in external markets. The fact that they are made means that we are allowing resources, which could earn the wherewithal to pay for our imports, to be used for new transfers or repayments of old debt abroad.

It is not easy to give the exact dimensions of this burden of capital export. But we know that it is large. The latest estimates for 1947 suggest that, on the most conservative accountancy, it was nearly £400 millions. (This was the year in which the Chancellor of the day described tentative queries whether something of the sort was not taking place as misinformed). Final figures for 1948 have not been published. But the provisional figures suggest something like £300 millions—significantly enough, not much less than the amount we were receiving by way of Marshall Aid. As for what has been happening recently, we know less. But two things are evident. First, that the increased rate of drain on the reserve seems considerably larger than anything which can be accounted for by current account transactions. Secondly, that there has been an increased rate of release of sterling balances. The recent settlement with India is a case in point.

These indications are serious. It is difficult to believe that the community at large is at all alive to their significance. They mean that we are using resources for capital export to a value of between a fifth and a sixth of our total imports, that at a time at which we have had to borrow abroad or solicit aid on a massive scale, we are in effect passing on a considerable fraction of the benefit in the shape of new loans or repayment of past debt. Whatever we may think of the justification of such a policy—and there will be much more to be said of this later—there can be no shadow of doubt that it has been a most substantial aggravation of the difficulties of our external account.

(*b*) *Inflation.*

The second factor responsible for the increase of our difficulties is domestic inflation.

Now inflation is an ambiguous concept : and there are many ways in which different kinds of inflation may affect the economy. Perhaps the most obvious way and the way about

which there is least controversy is its effect on prices and costs. Since the War, the level of retail prices has advanced from 148 (1938 = 100) to 179 and the level of wholesale prices from 166·7 to 228·6. We have no direct index of costs; but the Bowley Index of wage rates has moved from 154 to 193 and it is very difficult to believe that there has been any increase in productivity which goes at all far to offset this increase.

All this is tolerably well known; and, so far as the domestic scene is concerned, its consequences are sufficiently realized: the rise of wages, the increase of the general cost of living, the limping efforts of the salaried classes to catch up—these are recognized to be part of the inflationary process. In a vaguer way, those who give casual thought to these things must know that they are bad for our international position. It is customary even for Ministers to make some allusion to the disadvantages in external markets of a rising level of costs.

What is not generally realized, however, is the nature of the opportunity we have missed. Yet in fact it stands out conspicuously. In the period since 1945 prices and costs in the United States have also risen considerably. The B.L.S. Index of Commodities prices other than Farm and Food has risen from 123 in 1945 to 182 in May, 1949. We have only to reflect on the difference that it would have made to our competitive position if, while U.S. prices had risen to this extent, our own had remained relatively stable, to see what we have missed by inflation. The entire situation would have been different. What has to be done now by an extensive change in the rate of exchange, would have occurred automatically as a result of American inflation and our prudence. Throughout the inter-war period when doubts were expressed concerning our position in international trade, the one prime *desideratum* on which all of us were agreed was a rise in the American price level reflecting in some measure the favourable balance of payments. If anyone had told us that it had been revealed to him (authoritatively) in a dream that the American price level of goods other than Farm and Food would rise, as it has risen since the War, we should have sent out for drinks. We should have felt that we were sitting pretty. Well, they have risen in this way. But, because we have let ours rise too, we have to face a sterner form of readjustment. The decision to devalue the pound by thirty per cent. is a

direct consequence of our failure to control internal inflation.

Considerations of this sort tend to put many of the phenomena of the general so-called Dollar Shortage in a light in which, so far, it has not been at all usual to contemplate it. There is much talk about this problem. Vast tomes of statistics are produced to exhibit its exact dimensions. The ingenuity of the experts is continually in operation to attempt to assess the precise weight to be assigned to the various circumstances adverse to the economies of Europe, Asia, South America and elsewhere which have made it harder for them to earn dollars. But the number of times on which mention is made of the fact that many of the economies concerned have allowed themselves to inflate even more than the United States of America is very much less frequent. Yet surely this must be regarded as one of the main features of the situation. No well-informed person will wish to deny the difficulties in which some (though not all) of the countries now suffering from dollar shortage were placed by the damages and dislocation of the War. But very extensive resources were at the disposal of most of these countries or were made available by relief grants or loans from the United States. If it had not been for the local inflations, it might still be that these funds would have been inadequate to establish full equilibrium yet awhile. But it is quite certain that they would have been much less inadequate than has actually proved to be the case. To discuss the under-supply of dollars without discussing the over-supply of the other currencies is to discuss Hamlet without the Prince of Denmark. To make the United States mainly responsible for what has happened, despite the rise in the American price level, the considerable reductions in the American tariff and the pouring out of dollars in the shape of loans and subsidies on a scale without precedent in time of peace, is a very shabby falsification of history.

To return to our own difficulties. The effects of inflation on the balance of payments are not limited to direct effects on relative prices and costs. Even where prices and costs are under control and are held steady by public regulation or private understanding, inflationary pressure is still an obstacle to the equilibrium of the balance of payments. For inflation is in essence a tendency to spend on consumption and development at a rate greater than the rate at which consumption and development goods are forthcoming, as measured at current prices. When this is taking place, there is a tendency to deflect

for domestic purposes (either consumption or development) goods and services which otherwise would be available for disposal in export markets. It is not enough for prices and costs to be steady. It is not even enough for the exchange rates, at which these prices and costs are translated into terms of foreign moneys, to give reasonable scope for successful sales. If there is inflationary pressure, in the sense defined above, the volume of exports will tend to drop short of what is necessary, while the volume of imports, unless most rigidly controlled, with be continually tending to rise.

All this is tolerably well known by now, even if it is not always made the basis for ministerial decision. Since the crisis of 1947, it has not been a matter of serious dispute that, no matter whether there is budgetary equilibrium in the narrow sense, if there is not equilibrium in the general sense of a tendency for overall expenditure and output to be equal at stable prices, then the balance of payments must suffer.

What, however, is not so generally recognized is the probability that, at the present time, a process of this sort is still active. Our financial history in recent years seems to fall into three periods. There is first the period from the death of Keynes to the great crisis of 1947. About the inflationary tendencies operative then, there is now no reasonable question. Under a Chancellor who could profess to be astonished at "the contrast between the great difficulty of the overseas position and the relative ease of the purely domestic financial position," there was a complete divorce between financial and general economic planning. We indulged in the crass folly of the ultra-cheap money policy; and consumption and investment were allowed to develop on such a scale that that part of the American loan, which was not being passed on by way of capital export, was used up long before it was anticipated, the development of exports being quite inadequate to reduce the gap to manageable proportions. There followed a period of retrenchment and reform. The investment programme was pruned. A real (as distinct from an illusory) budget surplus was planned and achieved. While all this was on a more modest scale than the advocates of this policy might have wished,[1] its success was at least equal to expectations. The sense of internal pressure slackened. The volume of export

[1] Writing in this *Review* in October, 1947, I recommended a surplus of "five to six hundred millions."

activity increased in a manner that was distinctly promising. This was the second phase of post-war financial history.

For the last few months, however, it appears that we have passed into a third phase, in which inflationary pressure is once more renewed. For some time it had been apparent that the mounting volume of public expenditure was likely to make grave encroachments on the Chancellor's ability to achieve a surplus. But the main political pressure, from the Right as well as from the Left, was all in favour of tax reduction, without specifying how it could be carried out without involving further inflation. Hence when the Chancellor produced a budget in which these insidious and short-sighted pressures were resisted, the majority of economists were so relieved at his determination and so concerned to defend him against perverse criticism that they omitted to draw sufficient attention to the danger that the surplus for which he budgeted was very probably insufficient. Only Professor Paish and Mr. Tress kept their heads and, in a remarkable article in the London and Cambridge Economic Service Bulletin for May of this year which even yet has not received the attention it deserved, pointed out that, on the figures available, it looked as though the inflationary gap had reopened to dimensions of at least £100 millions *per annum*.

Since then developments have begun to justify these gloomy prognostications. The unemployment figures by themselves would suggest strong inflationary pressure. A state of affairs in which, with a working population of over twenty millions, less than one quarter of a million are unemployed is certainly something very different from what one would expect of "full employment" in the Keynesian sense with no tendencies to inflationary developments. When these figures are taken in conjunction with other developments these suspicions are greatly reinforced. During the summer there has been a marked contraction in the volume of exports. In a normal state of affairs it would be reasonable to expect that *for the time being* this would affect the unemployment statistics. That is not to say that the labour displaced would be permanently unemployed: only the ignorant or the malicious would suggest that this was a necessary consequence of the absence of inflation. But it would at least take a little time for the people concerned to find new jobs: and this would show itself in the figures. In fact this has not happened. The displaced labour has been reabsorbed almost instantaneously. There has been

hardly a ripple on the pool. For the greater part of the summer indeed unemployment continued to decline. I see no way of accounting for this save on the assumption of a renewal of inflationary pressure. Professor Paish and Mr. Tress were right.

The reason for this is twofold: the growth in investment and the growth in public expenditure. Messrs. Paish and Tress came to the conclusion that "true net capital formation is likely to be something like £200 m. more this year than last." The budget estimates for 1949–50 were nearly £140 millions higher than the exchequer issues for the preceding year. The real surplus of 1948–9 which, it is now clear, was never really large enough to give our position the strength that it needs, bids fair to dwindle to proportions which are quite inadequate to finance the capital formation contemplated.

These changes are the result of policy. But let no one make the responsibility a matter of party recrimination. I have seldom heard any attacks from the Opposition on the volume of planned investment, especially when the most vulnerable form of investment, the so-called social investment, was under discussion. As for expenditure, all Oppositions attack expenditure. But, although there have been honourable exceptions, this Opposition, at any rate, has not avoided the inconsistency of attacking expenditure in general, while promising the maintenance or even the increase of most detailed items thereof. The vital issue at stake in a recent election was which of the two parties would provide the more houses. I have yet to learn that the Opposition candidate gave any reason for supposing that, although he would provide more, he would spend absolutely less. We have heard a good deal of the desirability of economizing on the food budget; but the Opposition has recently been at pains to inform us on huge posters that what is in mind is, not any increase in the price of food, but more economical buying and administration—which of course makes hay quantitatively of any but the most modest expectations in this connection. The fact is that since the War the majority of the community, whether Conservative, Liberal or Labour, have been living in a fool's paradise concerning what we can afford; and the majority of their leaders, whether Conservative, Liberal or Labour, have done little to correct the delusion. There are a few who, like Sir John Anderson and Lord Brand, have consistently warned us. If

they care to say " I told you so " they will certainly be within their rights; for they have been shamefully attacked and misrepresented. But, for the rest, the less said about the past the better. Most have fallen short of the minimum survival standards of democracy.

(*c*) *Production and Incentive.*

Let us turn for a moment to consider influences on production.

It follows from what has been said already that the volume of production has been insufficient to offset the increases that have taken place in money incomes. That indeed is one of the most intelligible descriptions of the fact of inflation: if production were to keep pace with money income, there would be no increases of prices in general and no general increases of costs. When we say, therefore, that there has been inflation (and, with inflation, the embarrassments which follow, other things being equal, in the balance of payments), we say that production has been inadequate in this sense.

But, of course, this is not to say very much. When there is no further reserve of capacity, production can only be increased by hard work and intelligence; whereas the volume of expenditure can be increased by ministerial directive. It would be a severe criterion of the efficiency of productive arrangements to demand that, whatever the follies of elected persons, the efficiency of production should be such as to wipe them out. What we want to know in this connection, therefore, is not why production has not offset financial mismanagement, but rather whether, in the circumstances, the volume of production has been all that it might have been expected to be.

Now on this point it is important to retain some sense of proportion. It may be said with some confidence that the alarmist reports, current in certain parts of the foreign press, of a vast falling-off in productivity all round are not true. I would not feel so confident that these reports were not justified in the case of certain industries—building, for example. But, by and large, I am fairly sure they are not true. I have not much faith in the general indices of production. But I do not believe that they go as wrong as all that.

Against this, however, when Ministers and official propagandists sound pæans of praise at our so-called " effort," when

no less a person than the present Chancellor refers to it as "magnificent," I must confess that I am at a loss to understand their enthusiasm. It is true that the index of production is considerably above pre-war. According to the London and Cambridge Economic Service, the index for 1948 was 120, 1935–38 being about 108; in June this year it was 125. But the volume of employment is also above pre-war—exactly how much it is difficult to determine because of a change in methods of collecting statistics—which means that the increase in productivity per head, measured this way, is less; and of course it is productivity per head which matters. Mr. Aneurin Bevan, the other day, used a figure which suggested an eight per cent. increase. Assuming that this is correct, it is really not at all spectacular. If we are to maintain our position in the world, let alone make any progress, it is necessary to do much better than this. And when we leave the figures with their specious precision and look at facts which are known to all, the same impression emerges. When we reflect that this period of desperate emergency has been marked by the adoption of shorter hours and more holidays, the suspicion is reinforced, not merely that production has not been as great as might have been wished, but also that it has not been as great as it would have been legitimate to expect.

I wonder if anyone really doubts this in his heart? The five-day week is an amenity which is very desirable. But was it the happiest moment to adopt it when our reserves were depleted, when our assets were reduced and when, by common consent, a special effort was needed? Can anyone who has travelled abroad either in Continental Europe (where standards of life and capital equipment are inferior to our own) or across the Atlantic (where they are better) really maintain that in comparison we present the impression of an all-out struggle. The accusation that we are a castle of indolence is doubtless misplaced. But the claim that we are a hive of strenuous industry is also inaccurate. There is a certain mediocrity in what we do, an easy-going economy of effort, strangely out of harmony with the real perils of the situation.

In part this is probably a by-product of inflation. Inflation, of the degree to which we have been subjected, creates so intense a sellers' market for labour that, as in all intensive sellers' markets, there is a tendency for what is sold to deteriorate in quality. The threat of a possible rejection

of what is offered ceases to operate. The possibility of dismissal has always been held to be an indispensable instrument of discipline in industry, in nationalized concerns equally with those under private ownership. But, if nothing is lost by losing a job, this sanction ceases its effectiveness. This may sound a hard thing to say; and by the unscrupulous it will doubtless be said to imply a plea for widespread deflation and unemployment. But this will be a gross misrepresentation. To argue that it is bad to be in a high fever is not to argue that the temperature should be several degrees below normal. We get the contemporary picture quite out of perspective if we suppose that an unemployment percentage below two represents a normal state of "full employment." On the contrary, it is one of the surest signs of a state of inflationary pressure. Few things can be more certain than that such a state of affairs cannot persist for ever. But, while it lasts, the same force which imposes a direct drag on the increase of exports at the same time damages the situation still further by undermining industrial discipline.

Beyond this, however, although still connected with the root trouble of excessive expenditure, comes the damage to incentive which arises from the present burden of taxation. This operates in various ways. I myself have little doubt that, at present levels, a high flat rate on income diminishes the will to work; when work is so highly taxed, there is a strong disposition to spend more time on the untaxed good, leisure, or at least to spend it on forms of work (e.g. jobbing gardening at the week-end) which escape the net of the tax collector. I think this is borne out by general observation, although, analytically, it is not certain. When, however, the rate of taxation rises with increasing income then the findings of analysis and observation are unequivocal. If the longer or the harder he works, the greater the rate at which he is taxed, a man will tend to work less. It is surely common experience that the increasing marginal rate of taxation is one of the chief disincentives of our day.

Such a disincentive, wherever it exists, is a day-to-day drag on productivity. But, on a long view, its effects are probably most serious in the sphere of enterprise. If a man or a company is confronted with the choice between routine operations, with a more or less predictable return, or a venture into the unknown, where failure means loss of capital and success

the substraction by the tax gatherer of all but a small fraction of the gain, the temptation to continue with the *status quo* is strong. The point is so obvious that it needs no elaboration. But it is doubtful whether it is realized how damaging such a state of affairs can be in its cumulative effects. A society in which there is so strong an incentive against innovation and risky enterprise as there is in ours today, is a society which is in the gravest danger of falling behind in the increase of productivity. And to fall behind in the increase of productivity is just what we cannot afford today.

These considerations are especially relevant in a situation such as ours where one of the main *desiderata* is an increase in the volume of exports. Any drag on productivity is a drag on costs which, in turn, is a drag on export sales. But, over and above this, any deterrent to the taking of risks is a special deterrent to the search for new export outlets. It is a fallacy to suppose that increases of exports arise automatically, even if the situation be otherwise favourable. Export outlets are created by deliberate enterprise. The search for new markets is usually decidedly more hazardous than the cultivation of old ones. It is all very well for Ministers to get up at week-ends and make patriotic appeals to manufacturers to recognize the paramount necessity of exports. The experience of the last few years shows that manufacturers in this country are by no means deaf to such exhortations. But they are a poor substitute for the day-to-day incentive of possible extra gain. And it is just this incentive which tends to be deadened by a high marginal rate of taxation.

Speaking generally, it must surely be recognized that the conditions now prevailing in this country are the reverse of conducive to enterprise. At a time when we need enterprise and innovation more urgently than at any other period in our peace-time history, the whole tendency is to make the exercise of these activities more difficult. Everywhere the striking out of new paths is hampered by administrative control and legislative uncertainty; and these obstacles are but the sign and symbol of something deeper. With us, at any rate—I sense some change elsewhere—the spirit of the age is inimical to the spirit of enterprise: a levelling passion is abroad, restrictive of spontaneity. Distracted overworked men at the centre dictate and limit the activities of a periphery which becomes more and more apathetic. While this state of affairs

persists it is not easy to be optimistic about the rate of increase of productivity in the future, and it is difficult to believe that it has not adversely affected our rate of recovery, and hence our balance of payments, in the past.

III. Remedies.

(*a*) *Devaluation.*

The main action which has been taken by the Government to meet our present very serious difficulties has been devaluation of the pound from 4·03 dollars to 2·80.

Let me say at once that, subject to two very important *provisos* to be mentioned below, I believe this decision to be sound. I should not have said this while the sellers' market persisted in the world at large. While our deficiency of exports was a matter of production rather than of sales, in my judgement the balance of advantage lay in keeping the old rate. Doubtless this was not an unequivocal advantage; a lower rate of exchange would have meant a higher rate of profit in export business and hence a greater incentive to increase the volume of export production. Nevertheless, with the world in the state of confusion in which it then was, before any clear indication of competitive advantage and disadvantage had disclosed themselves, the dictates of prudence, it seems to me, lay in waiting to see how things turned out.

But once the sellers' market showed signs of disappearing and the extent of our competitive disadvantage in important markets became apparent, the balance of advantage shifted. It was fairly clear by the beginning of this year that the disparity in costs here and elsewhere was becoming such that only a change in the rate of exchange or a very severe deflation of incomes would serve to maintain the position we already held, let alone permit the further expansion of exports which is so urgently necessary. In such circumstances I have no doubt that it was right to choose devaluation. A change in the value of sterling is indeed a very serious and important step, not to be undertaken lightly. There is a great deal to be said for resorting to local contraction, rather than a change in the rate, when disequilibrium is of a minor order. But when the disequilibrium is large, then it is surely better to attempt to rectify it by a change in the rate, which leaves the internal income structure unaltered, rather than resort to contractions,

which can only prove effective after long agonies of internal readjustment, if in the meantime they have not produced a *bouleversement* of the entire political and social structure. If I were to criticize anything in this connection, it would not be the decision to devalue, but the delay in coming to that decision, which must have cost us many millions of our all-too-scanty reserves. It is hard to understand the leisurely frame of mind in which these urgent matters have been handled.

I think it is right too that once this decision was made, it was decided that the cut should be of sufficient magnitude to give reasonable assurance that, provided always that certain other measures are taken and the advantage is not frittered away, the new rate can be held. Nothing would have been more disturbing than a movement which the world at large judged to be too small. In this connection, it must be recognized that since a large number of other countries have devalued with us, the effect of any given cut in our rate on our export sales in dollar areas is to that extent reduced, although to the extent that their devaluations put them in a better position to pay us in convertible currencies this may well be more than offset. Moreover, it must be remembered that, in all probability, the full measure of the difficulties which we are likely to encounter in international competition has not yet been revealed. It is well to have some margin in hand.

What has happened in the last few weeks is in effect almost the equivalent of an appreciation of the dollar, though without the disagreeable consequences for gold mines which that policy would have involved; and, for reasons which were most forcibly set forth by Professor D. H. Robertson in the last number of this *Review*, on balance the change is to be welcomed. At any rate the burden of proof is with those who argue the other way. For let it be remembered that if it be argued that a downward movement of the rate of exchange of countries in disequilibrium would make things worse, the implication must be, other things being assumed to be equal, that an upward movement would make them better; and this does not seem to be plausible.

But all this is subject to the condition that the fundamental causes which have brought about disequilibrium cease henceforward to operate: that is to say, that inflationary pressure ceases and the export of capital is reduced to more appropriate proportions. If this does not happen any change in the rate

of exchange will be in vain. If costs in this country continue to rise, or if the vast sums accumulated here as a result of the peculiarities of war finance continue to be withdrawn at a high rate, no change in the rate of exchange will save us. We shall continue to be in disequilibrium. Our reserves will continue to fall and within a measurable distance of time, we shall be forced to other policies by the sheer physical inability to buy what we need. But this process will involve short commons and widespread unemployment.

For this reason many of us would have felt happier if the change in the rate of exchange had been preceded by the other necessary changes in policy, retrenchment at home and some settlement of the problem of the sterling balances. At the present time we are in the position of a patient who needs two surgical operations, one easy, the other very difficult. The easy operation has been performed. But it will only be effective if it is accompanied by the other: and it is not sure whether the patient is going to submit himself to the second or whether, even if he is prepared to do so, the surgeons will have the nerve and the skill to perform it. Meanwhile, whether he knows it or not, he is in a position of extreme danger.

It is clearly incumbent on all of us, therefore, to try to think out exactly what is needed.

(*b*) *Disinflation and Internal Finance.*

Let us look first at internal finance; if that is not in order, everything else is bound to go wrong. It is fundamental to take all traces of inflation out of the system; if that is not done the advantages of devaluation can be wiped out in a very few months or even weeks. It is desirable, too, to restore some greater degree of incentive to work and enterprise; for although the weakening of incentive does not show itself in immediate collapse, in the long run it must produce a further deterioration of our position in relation to more vigorous and efficient communities and so lead to further difficulties and further crises.

To do this it is necessary, in my judgement, to make reductions both in the volume of investment and in the volume of public expenditure.

So far as reductions in investment are concerned, I should like to make my position clear beyond the possibility of misunderstanding. I am no foe to investment. I accept the view

which has been forcibly urged both by Professor Paish and Professor Viner, that there are large sectors of our economy where in all probability the volume of investment has been less than would be considered desirable, having regard to reasonable expectations of progress. But this view is not incompatible with the view that the volume of investment in general has tended in recent years to be too large; there are branches of the so-called civil investment sector where I am sure that outlay has been too lavish. Moreover, it is not incompatible with the view that, in present conditions, there is not sufficient selectiveness in the investment process. In a time of capital scarcity, such as almost inevitably follows a great war, it is desirable that investments which yield quick returns should have priority over those whose return is longer maturing. It is more important to repair vehicles and rolling stock than to provide new roads or permanent way. I think there is considerable evidence that hitherto the investment programme has not been framed sufficiently with this principle in mind. To that extent, therefore, there will be elements in the present volume of investment which can rightly be regarded as dispensable—even though later on, when the capital scarcity has diminished, they may be very good investments indeed. What is needed is some general impersonal instrument of selection which will sort out the more urgently needed from the less.

For this purpose, I think the experience of the last few years tends to show that we cannot afford to dispense with the mechanism of the structure of interest rates. I am far from urging that this is the only instrument we should rely upon—there will be more to say about that a little later. Nor do I wish to over-emphasize its efficiency in all situations that are conceivable or in all parts of the economic system. But I would urge that experience of a time when interest rates have been held at levels quite out of relation with the contemporary scarcity of capital does suggest that the substitutes for higher rates to which we have recourse are not sufficient by themselves. I therefore come to the conclusion that, for the time being, in spite of its possible disadvantages in regard to public finance, it would be appropriate for steps to be taken to put the long term rate of interest up.

In this connection, I cannot forbear from alluding to what seems, at any rate at first sight, to be a palpable inconsistency in Government policy. Since the autumn of 1947

disinflation has been the accepted principle and, so far as the budget and the investment planning are concerned, some attempts, although inadequate, have been made to put this principle into practice. But in the narrower sphere of finance one looks in vain for parallel operations. The volume of deposits is clearly a matter which is completely within the control of the Bank of England; the joint stock banks at large are purely passive agents in regard to this total. Yet at a time when disinflation has been preached and (occasionally) practised elsewhere, a not inconsiderable expansion of bank deposits has been allowed. More surprising still, at a time when the reserve has been flowing out at a rate which was alarming to contemplate, there seems to have been no attempt to use the traditional instruments of monetary policy to prevent this happening. Many of us who listened to the Chancellor announce the most drastic devaluation in our history must have confidently expected that, before the end of his speech, there would be announced an increase in Bank Rate—a sign to the rest of the world that we had not only decided on a new value for the pound but that we were prepared to fight to defend it. But these expectations were not fulfilled. The nationalization of the Bank of England clearly precludes the attribution to that institution of independent initiative in policy; and the officials of the Bank must henceforward be regarded as possessing the same complete immunity from criticism as other members of the public service. But it is at least permissible to suggest that the Chancellor, who is now to be regarded as solely responsible for ultimate decisions regarding policy, has not as yet succeeded in bringing about so complete a harmony between his actions in different capacities as might be desirable in the public interest.

To charge higher rates when private enterprise borrows is obviously not enough. In the large sector of investment which is directly controlled by the Government, it is desirable that a similar selective principle should apply. Even where the Government does not have to pay higher rates on the funds at its disposal, it should judge alternative investment plans as though they were subject to this obligation. That is to say, it should reject the projects which do not promise a yield at least equal to the rate which is laid down as the criterion. Even in that sphere of social investment, where the computation of benefits in terms of cash is manifestly out of the question, it should be realized that the least urgent types of cases, which

were sanctioned when easier conditions were assumed to prevail, must become extra-marginal now. Indeed, in my judgement, it is just in this sphere where the most considerable reductions are possible. There are many projects of civil development now in process or in contemplation which might well wait until we are faced, as we shall be later on, with the necessity to offset a spontaneous decline in investment.[1]

The extent to which it is necessary to cut investment, the extent therefore to which it is necessary to raise interest rates, obviously depends on the extent to which it is found possible to create a real surplus in the budget. The larger the surplus, the larger that is to say the volume of forced saving, the less the need for cuts in the investment programme. While sharing Professor Robertson's scepticism concerning the prudence of relying exclusively on the policy of the budget surplus as a substitute for the rate of interest, I am clear (as I fancy Professor Robertson is) that we cannot afford to dispense with this policy. The level of interest rates which just now would be necessary to prevent inflation, without a budget surplus, would be very unpleasant to contemplate. In our present predicament we cannot afford not to be eclectic in our financial policy.

But to create a budget surplus in circumstances in which, by common consent, the burden of taxation is at a level which itself is damaging to enterprise, it is necessary to cut expenditure. And if it is desired both to achieve a surplus and to permit some reduction of taxation it is necessary to cut expenditure even more. I am convinced that such cuts are necessary. The present volume of expenditure is one of the greatest threats to our recovery; and policies to which we are already committed bid fair to increase this burden. Disagreeable as it may be, we have to face the fact that we have tried to do too much too soon and that if we are not to endanger our hopes of further progress we must, for the time being, reverse the process until we are in a better position to afford what we hope to do. A considerable reduction of public expenditure has become a prime necessity of national safety.

[1] It is obvious, if these principles are applied, that there will be some cut in expenditure on housing. No pruning of the investment programme which took its job at all seriously could leave so extensive a branch of total investment untouched. In judging the significance of this it is important to realize that it need not imply a reduction in the number of dwellings. All that is necessary is that the standard should be temporarily lowered. This is not nearly so terrible as it sounds. I think it would be found that a return to standards, which, in the inter-war period, were considered quite acceptable, would release a significant amount of resources for other uses.

For this reason, we must applaud the news that a serious attack is to be made on the general expenses of administration. It is indeed possible to exaggerate the economies which are possible in this direction. But it is not true that they are small.

Nevertheless this is not enough. We deceive ourselves if we suppose that the position can be made really safe by economies which involve no general changes in policy. It is only necessary to look at the composition of public expenditure to realize that this is so.

For this reason I cannot but deplore the type of all-or-nothing statement which is being made in many quarters, with regard to the social services. Even Sir Stafford Cripps, to whose realism and sense of public duty we owe so much, seems inclined to suggest that the present volume of expenditure on the social services is something completely sacrosanct, and that no policy of judicious economy here and there is possible without the ruin of the whole structure.

Such an attitude is surely unjustified. It is unjustifiable to contend that every item in this vast structure is equally indispensable. It is unjustifiable to contend that nothing can be cut without causing serious hardship and the collapse of all our hopes of improvement. It is not conducive to the calm consideration of the whole position, which is so essential if we are to extricate ourselves without the impairment of national unity, to argue that anyone who mentions the possibility of cuts in this connection is an enemy of humanity and progress.

Take, for instance, the example of food. It is just not true that extreme and extensive hardship would be caused if the prices of some of the subsidized commodities were allowed to rise a little. The arguments which are commonly employed in popular discussion of these matters are really an insult to our intelligence. In a community in which the expenditure on food is only a little more than a quarter of consumption expenditure in general, it is unreasonable to argue that there is not some margin for increases which do not cause grave hardship. Apparently it is necessary to remind ourselves that we are not still in the early days of the industrial revolution when a large proportion of the population really lived at the margin of subsistence. It may be that at the very bottom of the income scale there is a small group whose position would be embarrassed. But there are many ways of looking after that besides

subsidizing the consumption of all of us: some change in family allowances, for example.

Or again, take the Health Service expenditure on which has reached such unexpected, such enormous, proportions. Is it really sensible to argue that nothing can be done here to relieve the strain which would not ruin the whole scheme? Surely not. On an earlier occasion Sir Stafford himself has hinted at the possibility of putting the scheme on a fee-paying basis. It does not need much imagination to see that a very modest innovation of this sort would greatly change the situation. It would yield a substantial sum to the exchequer: it would be a deterrent to frivolous visits. Yet who can contend that the majority of people would be gravely impoverished if they had to sacrifice the price of a few cigarettes any week that they called on the doctor?

Are these things impossible? I do not know; for possibility in this sense is a matter of will and persuasion. But two things are plain: first, that there exists a wide range of possible devices of the kind which have been cited above which, had we the will to adopt them, are at once administratively practicable and capable of bringing substantial easements to the budget without involving serious hardship; secondly, that if we do not do something of this sort our financial problem will continue to be unsolved and our position in the world at large will continue to be perilous.

(c) *The Sterling Balances.*

Even if we put our internal finances in order and remove all traces of inflationary pressure from the system, our external account will still be under grave pressure, if the export of capital continues at the level of recent years. To have to make exports (or to borrow abroad) to the tune of £300 millions a year or more to make possible new transfers or the repayment of old debt is a burden which we ought not to assume. It is a burden, moreover, which in all probability would never have been voluntarily assumed by the community at large if the community at large had known what it was doing. Public personages may from time to time boast of the vast assistance which we have rendered in this way in recent years; and unreflecting audiences may cheer. But if it were generally realized that thereby our own imports of food and raw material would have been jeopardized had we not found kind friends

elsewhere to help us stagger on, it is hard to believe that the cheers would be very vigorous.

So far as new capital export is concerned, we may assume that there are means available to limit the volume of transfer. If interest rates were somewhat higher and if internal uncertainties were less, it is doubtful whether, in the present troubled state of the world, the volume of new capital that would voluntarily leave this country would be excessive. Even if this were not the case—and until the domestic prospect improves, it would be dangerous to under-estimate the desire to move—existing mechanisms of control should be sufficient to keep the movement in check.

But the repayment of past debt presents another and very special problem, the so-called problem of the sterling balances. So long as there are outstanding the abnormally large balances accumulated during the War by governments and persons abroad, whose withdrawal is limited only by special arrangements made *ad hoc* at frequent special negotiations, so long will the situation have an incurable instability and uncertainty, utterly inimical to the restoration of more normal conditions. It is not only that with the type of temporary settlement which at present prevails in this field, our negotiators (i.e. the Chancellor and other Ministers concerned) seem chronically unable to refrain from making concessions which are obviously out of all relation to what is prudent—witness the amazing terms recently accorded to India—it is also that while there is this abnormally large volume of " old " sterling about in the world, it is almost impossible to make any real progress to the re-establishment of convertibility. Until this problem is settled on a more permanent footing, it is safe to say that we shall have to continue to endure exchange control of the most ferocious nature and that nevertheless our balance of payments will continue to be in jeopardy.

Now it is not to be denied that this is a very difficult and delicate matter. While we discuss it mainly on the plane of moral deserts and obligation we are not likely to get anywhere. From our own point of view, on this plane, the thing may appear to be simple. We did not incur the expenses, in respect of which these balances arose, for any narrowly selfish purpose. The money was spent in a common cause and we feel that it is unfair that we alone should bear the burden. There is something repugnant to the most elementary sense of equity

that we should be endangering our whole position in the world, to repay monies whose expenditure made possible the victory of Alamein.

But this is only one side of the picture. There is no doubt that we hired the money, in the sense that we bought goods and services and paid for them in sterling. It is improbable that we should have got what we wanted on other terms. We feel that the money was spent in the common interest of humanity in preventing the domination of the world by Nazi and Japanese aggression. But it is gratuitous for us to assume that these feelings are necessarily shared by the creditors, not all of whom may have felt the same intense inner compulsion to sacrifice all rather than surrender. Moreover we must not let the difficulties of the moment obscure the fact that, in many cases, we, the debtors, are comparatively rich while they, the creditors, are absolutely very poor. It is not easy to believe that we can get very far while we merely bandy moral arguments with each other.

There are, however, practical considerations of a more generally compelling order of cogency. It is quite certain that not all the abnormal balances could be withdrawn at once without shipwreck of the whole structure of which they are part. If the attempt were made, we should be obliged to put up the shutters. It is also certain that we cannot repay at more than a very modest rate per annum—much more modest than the bountiful rates accorded recently—without imposing strains on conditions here which, when realized, would be thought to be intolerable. The present state of affairs just cannot last.

I conclude, therefore, that, although there should be no question of repudiation, there can be no obligation to repay at a rate which endangers our general stability. We must safeguard the interests of the whole body of creditors against the precipitate action of any group. This means in practice that, having made some more or less arbitrary segregation of the abnormal extra foreign balances accumulated during the War, we must quite definitely declare them to be inaccessible save at a certain rate, subject to waiver of the type prevailing under the terms of the first American loan, and only susceptible of modification in the case of those creditors who, like Canada and the United States, are prepared to regard the debts as being on a less commercial basis and make some definite scaling down.

Admittedly, a policy of this sort must give rise to all sorts of difficulties in centres which have based their plans on the prospect of a rapid withdrawal of the balances. It is to be feared that in certain centres something amounting to major investment inflation has been allowed to develop on the strength of expectations of this kind. Moreover, despite the fact that more rapid release creates intolerable embarrassments here at home, it cannot be denied that there are political considerations which make it very difficult to discontinue the process.

I have sometimes wondered, when listening to this kind of argument, whether an alternative settlement is not possible. Since so considerable a proportion of the yearly aid which we receive from the United States is passed on, directly or indirectly, to the sterling creditors, might it not be a good thing if, forgoing perhaps that amount of aid (which does not in fact accrue to our private advantage), we were to ask the United States to be directly responsible for a certain share of the balances and to make her own arrangements with the creditors concerning the rate of release. I used to think that it would be preferable, if we could settle this question ourselves. But I can see profound advantages in having it negotiated by a third party. I do not think United States negotiators would be so squeamish as ours in asking for some scaling down of the total amount; and, having regard to what they would have to offer, I do not think they would be so unsuccessful.

In any case, if the authorities of that much-pressed country feel that they have any further resources which they are prepared to devote to the furthering of a general international settlement, I can think of few ways of using money which would be likely to be more fruitful than this. It would break the log-jam in the progress towards convertibility. It would promote development in areas where, in the absence of some such arrangements, development would certainly be retarded. It would open to United States traders markets from which at present, by reason of the necessities of our present policies, they find themselves shut out.

All this may be wishful thinking. What is not wishful thinking, however, is the contention that the state of affairs which has prevailed up to now in regard to these obligations cannot be allowed to continue. Two years ago when some of us ventured to draw attention to the dangers of the policy then

in vogue in regard to the Sterling Balances, we were thought very wild fellows indeed. Today I believe the view that there must be some change is held by most serious-minded people.

IV. International Considerations

I must not bring these notes to an end without one concluding reflection on international policy.

From time to time, since the end of the War, Ministers have stated that our ultimate objective in international financial and commercial policy is the restoration of multilateral trade and convertibility of currencies. At the talks this summer with American Ministers these sentiments have been reiterated.

Nevertheless it is hard sometimes to resist the impression that it is all more the repetition of a formula than the expression of a strongly-felt intention. We say we are in favour of these things; yet it is difficult to believe that our actions assume them as compelling necessities of policy: if it were so, we should surely have done more; we should have tried harder to recreate the conditions in which some progress towards the goal was possible. And when we pass from the pronouncements of Ministers to the small talk of political discussion it is impossible not to recognize large bodies of opinion which, so far from wishing to achieve this objective, in fact wish to move in exactly the contrary direction. Each successive crisis is hailed as providing the pretext for finally going back on our promises and seizing the occasion to build a different kind of world, a world of regional blocs, bilateral agreements, tied finance and discriminatory trading.

In this respect there is little to choose between the parties. On the Left, the impulse springs partly from a congenital dislike of the American economic system with its disconcertingly efficient free enterprise, partly from the feeling (which has much to justify it) that, in the last analysis, there is a certain incompatibility between multilateralism and convertibility and the type of planning which has been recently in vogue in this country. On the Right, it springs partly from motives of prestige—how desirable it would be to build up our *own* economic bloc—partly from the lingering influence of the old ideology of protectionism and preference. If the ghost of Ramsay Macdonald is a powerful influence deterring Labour Ministers from recognizing their plain duty in this crisis,

the ghost of Joey Chamberlain is a powerful influence deterring Conservatives from recognizing the changed facts of the twentieth century.

But if we consider matters calmly and cast away doctrinaire prepossessions, it is difficult to avoid the conclusion that all this is very mistaken. The policies of economic regionalism and discrimination are not in our long-run interest, either economic or political. They may be plausible as the desperate expedients of a confused transitional situation. But if they are made the basis of long-term planning they are likely to complete the destruction of our general position in the world.

They are not in our economic interest for two quite distinct reasons. In the first place they are inherently unstable. I do not believe that anyone who has administered the system whereby we attempt to compel people to buy from us goods which they don't particularly want in return for promises on our part to buy from them goods which we don't particularly want, all in the interest of bilateral balancing, can believe for long in its ultimate survival value. The idea that we can build up stable connections whereby other countries continue to buy our relatively high-cost goods when relatively low-cost goods are available elsewhere, is a snare and a delusion. This is a danger which more and more is likely to force itself on our attention; there is so much talk about our difficulties in dollar markets that we tend to forget that difficulties in other markets are developing too and will continue to develop if we cannot maintain ourselves in international competition. In the immediate past it may have been possible to put up some justification for arrangements of this sort because of the over-valuation of sterling and other currencies *vis-à-vis* the dollar. In such circumstances there is a real argument for the case that arrangements which discriminate against dollar goods, may prevent a contraction of trade. But, with the general revaluation of currencies, this argument loses its justification; and the precarious nature of arrangements which are based on exclusion is likely to become more and more apparent.

In the second place, this type of policy is contrary to our interest because it is likely to provoke retaliation and to interfere with forms of co-operation which promise much more for the world. Just at the moment we hear a good deal about the consolidation, on a basis of exclusion of dollar goods, of Europe and the Sterling Area. But, quite apart from the fact

that there are difficult clashes of interest between the countries concerned, it is too simple by half to believe that we can go very far along this road and expect either that the Americans will go on financing such operations or will show any enthusiasm for continuing to lower their tariffs. The fact is, as Sir Eyre Crowe recognized long ago in his celebrated memorandum on the basis of British foreign policy, that the Empire or Commonwealth is an association which can only be held together on a predominantly *non-exclusive* basis. Any attempt, singly or in concert with a small group of Western European Powers, to make it a closed system is doomed to disaster from the outset. More than any other Great Power our economic interest in the long run must stand or fall with multilateralism.

But there are even more important political reasons why we should eschew these follies and continue on the course which we have adopted in common with America. Our supreme interest in this world is the preservation of peace and the safeguarding of the values of western civilization. The idea that this can be done without the closest and most continuous co-operation with the United States is silly. The idea that such co-operation can be maintained between two Powers or groups pursuing radically different economic policies in the international sphere is dangerous. The Americans have been very willing to make allowances for all the special devices which have been forced on us by the difficulties of the transition period. But if we were seriously to deviate from our promises to pursue identical final aims, it would not be long before we began to drift apart.

Let us hope, therefore, that the discussions which have recently taken place at Washington, if they have done nothing else, have restored our determination to let nothing come before co-operation between the United States and the Commonwealth. We must not allow ourselves to be deluded by the will-o'-the-wisp of the Third Force. To preserve the Atlantic Pact and to build upon it must henceforward be the chief objective of policy in the international sphere.

V. Conclusion.

For the moment, however, our main attention must be directed to preventing our economic position so deteriorating that what we do in the international field does not matter very

much to anyone. These notes must end as they began. Our situation is very serious. While we are still receiving immense subsidies from the United States, we have reached a point at which our reserves are dangerously depleted. The policy which we have adopted to meet this situation, the devaluation of the pound, by itself is quite inadequate. Unless it is accompanied by other measures it may positively increase the danger. We are now in such straits that it is quite impossible to predict with any certainty whether we shall still be solvent in a few months' time. Our standard of living, our savings, our general position in the world, are in grave peril.

To remedy this no one solution will suffice. We need to operate on a wide front with a variety of expedients. But there is one measure without which all the rest will be in vain, the definite elimination of inflationary pressure. To stop inflation, to cut down excessive expenditure, that is the supreme need of the day. The technical difficulties of doing this are not great; in present circumstances there are abundant means of preventing unwanted deflationary developments. It is only our own states of mind which stand in the way of an expeditious handling of the situation; the obstacles are all psychological. Unfortunately, states of mind can be as intractable as any material obstacle. It is still an open question whether we shall have the sense and self-control to put our house in order in time or whether we shall only learn to do so through bitter experiences in which many of the things, which have hitherto made our society, for all its faults, more tolerable than most societies in human history, may well be irrevocably destroyed.

LIONEL ROBBINS.

The London School of Economics.
3rd October, 1949.

Benelux

By The Editor

Introduction

UNTIL the reign of Philip II of Spain the Seventeen Provinces of The Netherlands, which included part of the old Burgundian inheritance, had for many a long day formed a political entity comprising in its orbit the most flourishing commercial and industrial centres of the world, and, amid the greatest variety of condition and development, the most progressive economic life of that age. In the revolt against Spain the Ten Southern Provinces (roughly modern Belgium and Luxemburg) had been unable to maintain themselves against the armies of Philip II, while the Dutch inhabitants of the Seven United Provinces to the North had not only driven the Spaniards out, but gradually pushed forward across the rivers and annexed the Northern part of Brabant around Bois le Duc or 's Hertogenbosch, the Northern part of Flanders which forms one section of the Southern bank of the River Scheldt, and an isolated district of Limburg. Reference to the map will give a clearer and more rapid conspectus of the position than is possible in narrative prose.

What could be more natural than that earlier Netherlands unity and prosperity should be recalled in 1940–44 by the Belgian and the Dutch Governments during their exile in London? There had, it is true enough, been some unfortunate happenings since the territorial scission of the 16th century, with the Dutch holding at times a winning advantage in navigation of the Scheldt and in economic exploitation of Belgium, for religion though the most prominent and embittering element in the quarrel had not been the sole operating motive. Yet great calamities provoke in the end countervailing efforts, and are found in the last account to have some compensations. In a world such as that of the early nineteen forties, racked and disturbed and of steadily increasing chaos, there is much evidence that the Western Governments were mainly inspired by the idea of the public good and the whole humanitarian side of politics. It was a situation which required a world outlook, and, although vested and sectional interests might be expected to oppose union, statesmen exist to see the world through plain glass and to impose broad views upon those who are narrow.


BENELUX
SCALE:
0 10 20 30 40
MILES
NORTH SEA
FRISIAN ISLANDS
Emden
GRONINGEN
Groningen
FRIESLAND
DRENTE
NORTH HOLLAND
ZUIDER ZEE
VECHT
Ijmuiden
AMSTERDAM
OVERIJSSEL
UTRECHT
Leyden
Utrecht
YSSEL
THE HAGUE
SOUTH HOLLAND
GELDERLAND
Arnhem
HOOK OF HOLLAND
ROTTERDAM
LOWER RHINE
WAAL
Nijmegen
RHINE
Wesel
SCHOUWEN
HOLLAND
GERMANY
MAAS
ZEELAND
'sHertogenbosch
(Bois Le Duc)
WALCHEREN
Flushing
Tilburg
Essen
RUHR
Eindhoven
E. SCHELDT
NTH. BRABANT
Zeebrugge
Terneuzen
ANTWERP
Düsseldorf
Ostende
Bruges
E. FLANDERS
SCHELDT
Dunkirk
W. FLANDERS
GHENT
LIMBOURG
LIMBURG
Cologne
BRABANT
BRUSSELS
Bonn
LYS
SENNE
BELGIUM
Aachen
Lille
Tournai
MEUSE
LIEGE
HAINAUT
NAMUR
Namur
Mons
Charleroi
LIEGE
Arras
FRANCE
SAMBRE
ARDENNES
DUCHY OF LUXEMBURG
MOSELLE
LUXEMBOURG
SOMME
Trier
MEUSE
LUXEMBOURG
Saarbrücken
LLOYDS BANK REVIEW

A
fo
m
Ea
Be
en
co
Be
th

of
flo
of
w
of
in
co
co
di
ne
B
sp
b
ye
co
th
B
p
n
er
n
to
C
ru
sl
p
h
a
o
li
h
o

A great war cannot proceed without far-reaching consequences for human life, and the prime necessity was to provide by every means against the prospect of renewed aggression from the East in years to come. *L'Union Fait La Force.* The idea of Benelux, though often mooted before, now worked like an enchantment; and on the 31st October, 1943, a monetary convention was signed in London by the representatives of Belgium, The Netherlands, and Luxemburg, to be followed on the 5th September, 1944, by a customs convention.

The principal objects of the first agreement were to fix the official exchange rates of the Belgian franc and the Dutch florin and to determine the conditions for the reciprocal grant of monetary credits. The declared aim of the second agreement was to pave the way eventually to a complete economic union of the three countries. That of Belgium and Luxemburg had, indeed, already been in a very large measure attained despite considerable difficulties which patience and goodwill had overcome. As between Belgium and Holland certain very formidable difficulties were foreseen, for it was not overlooked by the negotiating statesmen in London that in many respects the Belgians and the Dutch are not one in temperament, nor spiritual experience, nor political requirements, and the fresh but transient political union which had subsisted for fifteen years after Waterloo had not rested upon any broad and real community of aim, sentiment, or policy, and the result was that the two peoples were always then on the verge of open enmity. But even after the failure of this renewed experiment in political union it had been realized by many that there were, nevertheless, incontestable benefits in economic union so that efforts, foredoomed to failure, had on several occasions been made to renew it both during the 19th century and later. It took the pressure of external danger to produce unanimity. Once more we had the experience that the wheels of history run rapidly in war, and processes which otherwise might be slow and gradual then become swift and vehement. In the prospect of common action and common sacrifice for a cause held to be great and sacred, dividing memories are laid aside and petty suspicions are discarded; possibly also vaulting optimism gains the ascendant and some real difficulties get lightly slurred over. But all that lay in the future. It was hoped that the deeper sense of unity which persists at the heart of European turmoils would find its embodiment in Benelux

and thus shine out in the post-war world like a lighthouse in a storm. Yet how little can the wisest statesmen forecast the future.

The whole landscape of public affairs, and the weights and balances of the world, were largely transformed not so much by the perversity of man as by the dollar gap. This factor was, as may be supposed, a major cause of disturbance and perplexity in Benelux as elsewhere. Belgium and Luxemburg found themselves in the dollar area, The Netherlands in the sterling area.

For all that, if at the end of the recent desperate contest, conducted on a scale far exceeding all previous experience, Belgium and The Netherlands had but emerged at one and the same time and on equal terms, it might have been possible, though in the changed post-war situation it could in no case have been easy, to launch Benelux on an even keel. " Heaven's will was otherwise." A tremendous disparity had been imposed by the stern pressure of circumstance, the implications of which, since they are costly and devastating, must be boldly faced.

The Governments have accordingly decided to proceed in stages spread over as long a period as may be necessary. If only they can gain a correct appreciation of the position it is not anticipated that they will fail in readiness to suit their action to it. The issues involved are highly complicated, and there is much to be understood before a right judgement can be formed. Meanwhile, according to various press reports, the wartime enthusiasm for Benelux has somewhat lessened.[1]

We hold no brief for the London negotiators. They may, perhaps, be criticized *ex post facto* upon the pretext that though keen of vision they were wanting in analytical powers. Possibly they might retort that the post-war critics are so concerned with passing squalls that they are blind to the polar star. All that can be attempted here, in Section II, is to set out the case for the defence in rough epitome. Then, in Sections III and IV, we pass to PROGRESS UP TO DATE and THE DIFFICULTIES. Finally, in Section V, entitled CONCLUSION, we have tried, in broad outline, to bring some of the main and long-term issues into true colour, light, and relation.

[1] See, *inter alia*, the record of an interview with the distinguished President of the Antwerp Chamber of Industry printed in *Vita* of June 30th, 1949. Undoubtedly it is a very difficult task to be alternately witness and judge ; to feel strongly, and yet to analyze coolly.

II. The Economic Benefits Anticipated

Now what precisely were the economic benefits which the London negotiators may be supposed to have anticipated from the entry into force of these conventions of 1943 and 1944? They were, undoubtedly, many and various, and may perhaps be listed in ascending order of importance.

i. *Collective Negotiating Powers*

There was in the 17th century a Dutch author, L. Aitzema, who wrote a history marked by the quality of its insight and the true balance of its judgement. After some sage reflections on the general infirmity of human nature, how everybody looks outwards, nobody homewards, and one and all are apt to claim a monopoly of the most elementary virtues, he pithily pictures what takes place:

> The big fishes eat the small ones; he who has the might uses it.[1]

The new Union of Benelux would, however, actually represent the world's third largest participant in international trade.[2] It will readily be imagined that—in a world dominated by huge political conglomerates such as the Soviet Union, the U.S.A. and the signatories of the Ottawa Agreement, not to mention the menace of a resurgent Germany apt to use the leverage of commercial enterprise for the promotion of political ascendancy—statesmen of Benelux representing some 20 million souls must *prima facie* speak with greater weight and authority in negotiation with third parties than would the individual representatives of Belgium, the Netherlands, and Luxemburg.[3] To take but one illustration, third parties might prove to be more considerate in any adjustment of currency values.

---

[1] Aitzema, L.: *Saken van Staet en Oorlogh in en omtrent de Vereenigte Nederlanden*, 1621-68. (The Hague, 1669-71. 6 Vols.)

[2] See statistical table on page 67.

[3] According to the United Nations' *Monthly Bulletin of Statistics* the following were the mid-year 1948 figures of population, with the average annual increases in the three preceding years:

Belgium	8,557,000	72,700
Luxemburg	292,000	3,000
Netherlands	9,794,000	177,300

According to the *Interim Report*, dated December, 1948, on the European Recovery Programme, the density of population per square kilometre in 1947 was 292 in the Netherlands, and 265 in Belgium and Luxemburg combined. The comparative figures given for the United Kingdom are 206, for Switzerland 114, for Denmark 99, and for France 74.

ii. *Increased Competition*

It must not be forgotten that there is no great distance between the main centres of population in Belgium and The Netherlands and that, with increasing freedom in the movement of people and currency over the common frontier, there will be an inevitable tendency for any price inequalities in the two countries to level off. Competition in all three participating countries, with its concomitants of growing adaptability and resiliency, would be intensified and this should result in a lowering of profit margins and consequently of retail and export prices over the whole Benelux area. Let it be conceded that the process would involve the fading out of some of the less progressive concerns whose protests may well be very vocal. You cannot attain development without disturbance. Here *il faut laisser travailler le temps*. Ultimately two criteria will be valid : (*a*) has there been a better distribution of available labour with a speed-up in individual enterprise and initiative, in technological progress and in the volume of competitive exports ? (*b*) has there been, in each of the three countries, any diminution of the net dividend for the community as a whole, or has there been an augmentation which is the basic condition of an improved level of life ?

iii. *Expansion of the Free Trade Area in the Internal Markets*

Although as between Benelux and the U.S.A. the analogy is far from complete, it is pertinent to observe that one of the formative factors of the prodigious industrial rise of the U.S.A. during the past 75 years lies in the vast and varied regions they comprise, not one of the States in this great land area being segregated from the rest by tariff walls. The mere size of the American market has stimulated technical specialization and favoured efficiency both in production and in trading operations. On a smaller scale, but on the same principle, we may partly ascribe the rising prosperity of England in the later 17th century and of Britain in the 18th century to the absence of internal tolls and to the fact that Britain was consequently then the largest free trade area in Europe. It will be recalled that Colbert fought unremittingly though with little success to abolish internal tolls and tariffs in France ; nor was the prevalence of such hindrances to internal trade the least among the causes of the economic

decline of Habsburg Spain. No unprejudiced mind can refuse to allow that programmes of commercial expansion would be larger—probably, to speak within bounds, they could be more than doubled—in the free trade area of Benelux than in the separate entities of Belgium, Holland and Luxemburg. The resources of all three countries are diversified, so that their activities are largely complementary and capable of a high degree of integration in a rounded economy. Belgium and Luxemburg have regional advantages in heavy industry. The Netherlands excel in agriculture and in light industry. This list could easily be extended. In foreign trade all three countries are in a front rank. The sea, a source of infinite refreshment, has ever prevented Belgians and Dutch, both amphibious communities, from being victims of a narrowing localism.

iv. *Expansion of the Capital Market*

It is well to examine each case under our consideration in the light of general arguments confirmed or rebutted by the broad facts of human experience. For instance, some seemingly intractable conflicts between the great oil concerns in the Middle East were overcome by a financial fusion of interests. The Dutch have an unrivalled experience in foreign investment, the Belgians are past-masters in the technique of holding companies. It is hardly conceivable that the total amount of available capital could not be distributed more efficiently, and invested more advantageously, within the wide ambit of Benelux than if the free flow of money were restricted by harassing exchange controls tediously at work between Holland on the one side and Belgium and Luxemburg on the other. Such a free flow of capital is a *sine qua non* of the division of labour if that process is to be applied and to receive all the success which it is capable of yielding. It might even prove the solvent for the age-long antagonism between Antwerp and Rotterdam, pour oil on the waters of the Scheldt, and facilitate inland navigation to Ghent and Liége.

v. *The Long Term View*

The experience of 1815–30 showed that these two excellent people, the Dutch and the Belgians, were incompatible in the sense that neither would ever stand being governed by the

other. Benelux on the other hand, in the changing industrial relations of the Eastern and Western Hemispheres in the post-war world, offers to its participants in all likelihood the only path of long-range economic survival, while preserving to each of them national independence in conditions of social contentment. The difficulties will be grave and the technical complexities very stubborn, but they are not necessarily insuperable provided we attack the task before us with resolution, minute assiduity, and, above all, with an inexhaustible store of that steady-eyed patience which is the sovereign requisite. Then the pooling and thrift of resources achieved over the whole Benelux economy would—if carried out upon an equitable and forthright basis—repay all concerned with an usury of profit beyond their most sanguine dreams.

Such, at any rate, is the thesis of many whose views, right or wrong, are these: that Belgium, Holland and Luxemburg have been behind their capabilities, not because their workers work too little but because their separatist set-up is so ill-adapted to giving full play to their aggregate economic potential in our modern and rapidly changing world. The facts of the case and the basic long-term problems are so cogent and compelling that, once they are allowed to emerge, level-headed, sensible people like the Belgians and the Dutch will certainly pay them heed.

The Economic Union of Belgium and Luxemburg, which began in 1922 and (apart from a total levelling of excise and sale taxes) was completed before the War, has shown by the logic of experience how a developing and overlapping economy can be guided and governed by two co-ordinate Sovereign States. Its supreme merit is that it works and has liquidated earlier failure in various directions. Indeed, its success to some extent inspired the idea of Benelux, though, of course, the circumstances are not parallel in several essentials, Luxemburg being land-girt and about the area of Derbyshire. The currencies of Belgium and Luxemburg are now freely convertible and a common monetary system is the mechanism through which the policies of one partner impinge on the economy of the other, so that any marked movement of prices

in Belgium, for instance, almost inevitably brings on a similar movement in Luxemburg. In practice, an economic equilibrium usually prevails over any discrepancies which may arise.

Of set purpose no attempt was made by the London negotiators to settle details; they could not enter into easy contact with experts in the home-lands; it was deemed but robust common sense to await the moment of liberation from the German yoke, the more so since details must in the last resort be entrusted not to politicians but to professional economists working under the good old rubric of scientific serenity. There is, however, evidence that these statesmen did take a wide survey of some of the principal difficulties in the way of policy though their emphasis seems to have been not so much on the difficulties as on the hope of overcoming them.

The final objective of Benelux as conceived in London was the ultimate establishment of full economic union. Had political fusion been in view (which it was not) it would have raised in its most acute form the central issue of paramount authority, and the Austinian doctrine that democratic government cannot be carried on in one area by two or more really equal and independent Parliaments. Full economic union, based upon a material welfare to which each of the member States would jointly contribute, meant that no economic barriers of any sort should be allowed to exist between them. Workers would be able to move freely from one country to another and not suffer in the level of social benefits by so doing. Money being, as Lord Stowell said, in theory and in fact an article of commerce, must be allowed to flow freely from one area to another within the compass of Benelux if no restrictions are to be imposed upon the free movement of produce and goods. From these premises it follows either that a single currency must be established for Benelux or if separate currencies are to be maintained they must be freely convertible and have equal stability in world markets. This involves similar customs tariffs, similar fiscal and monetary policies, interest rates roughly parallel for equivalent types of loans and investment policies more or less co-ordinated, and

unified controls of foreign exchange. Otherwise exchange rates, and with them price and wage levels, will be distorted. Port dues and railway tariffs must be equalized, and no grant-in-aid, such as subsidies, must be accorded in one region to the detriment and disadvantage of other regions. A full economic union of the kind aimed at is only possible if (*a*) each member State pursues more or less completely liberal trade policies and (*b*) each Government conducts its financial policies on a more or less uniform basis, and with due regard for the long-range interests of all three member States. Even if the union of two countries each pursuing a planned economy is conceivable in theory, in practice it would come up against grave and almost insuperable obstacles.

The immense difficulty of getting Europe to work together for a common end, which was felt so keenly by Sir Edward Grey in the earlier years of this century, has been illustrated in a most signal manner in The Low Countries when that century is now approaching its mid term. We shall not only see that the stars in their courses have fought against Benelux. We shall also feel that a swarm of minor difficulties have come to life as flies in the summer heat. Nevertheless Horace Walpole was right when he declared that prognostics do not always prove prophecies, and when we have pondered all the evidence a massive impression remains that the batch of difficulties have assumed an aspect a good deal more formidable than the reality. " If you believe the doctor," wrote a great Prime Minister, " nothing is wholesome, if you believe the theologian nothing is innocent, if you believe the soldier nothing is safe."[1] If we believe Bunyan's Timorous and Mistrust we shall see a lion in every path. Benelux carries the seed of much more than purely regional adjustments, vital as they are. Every believer in the noble art of preventive diplomacy, in both Hemispheres, should seize this opportunity to promote by every means constructive peace. And what finer monument, *aere perennius*, than Benelux could its member States raise to the memories of those who laid down their lives in the liberation of Belgium, The Netherlands, and Luxemburg?

[1] *Life of Robert, Marquess of Salisbury*, Vol. II, p. 153

We shall now briefly recount the progress which has been made up to date. We shall then analyze the stubborn difficulties which have been met with; these are historical and psychological, and they also stem from differences of economic policy and problems.

III. Progress up to date[1]

It had originally been planned to implement the London Agreements immediately upon liberation. This could not be done because Belgium was freed in a flash, while The Netherlands were the battle-ground of heavy fighting for another 8 months. Moreover it was found that considerable modification would be necessary in the common schedule of tariffs that had been hastily worked out in London and many obstacles had to be overcome and a new nomenclature, involving some 900 categories, was worked out. The Dutch customs tariff was primarily fiscal, on an *ad valorem* or percentage basis, and very low; the Belgian was specific and, generally speaking, protective. Nevertheless a new tariff, mainly on an *ad valorem* basis of between 3% and 24% of the value of imports, with some large categories of raw materials duty-free, was put into force early in 1948. The post-war period was a particularly advantageous time to reach agreement on common rates as most duties were completely suspended because at the end of the War Belgium and Luxemburg and The Netherlands were all desperately in need of imports from the outside world.

In order to implement their agreement for a tariff union and to prepare subsequent steps leading to ultimate economic union the member States of Benelux have established three Councils: (1) for Customs Regulation, (2) for Trade Agreements with Foreign Countries, (3) for Economic Union. A joint Secretariat headed by a Dutchman has also been established at Brussels.

On January 1st, 1948, the common customs schedule was put into effect, but its importance must not be exaggerated, though it is a first step towards the ultimate goal of full economic union and it does increase the bargaining power of the member States in respect to the rest of the world. It is instructive to

[1] The substance of the earlier part of this Section is derived mainly from the excellent discussion in *The Final Report on Foreign Aid* presented to the Committee of the Whole House at Washington on May 1st, 1948.

recall the comment of Mr. Van Zeeland in making his report to the Belgian Senate:

> It would be an error, however, to expect considerable and rapid results from the measure. Everyone knows that of all obstacles to international trade, the least important is still the customs duty. . . . If, as in this case, at the time we eliminate the customs duty we maintain between two countries quotas, licences, restrictions of all kinds, it is evident that the effect of the elimination of the customs duty can only be of limited nature.

In September, 1949, it was announced that the "pre-union" of the Benelux Economic Union is to be established on October 1st. During the pre-union stage a number of carefully listed commodities will be freely interchanged between the countries concerned.

Until the price levels in all the member States are more or less equal, so long as import and export quotas are in force on nearly every major item of trade, and until excise taxes, sales taxes, and other taxes have been equalized and economic controls have been removed, it will not be possible to attain complete economic union. It is, however, anticipated that The Netherlands will have got rid of all subsidies and rationing with the exception of textiles by the end of 1949 and that even the end of textile rationing may be expected in the near future. This means that The Netherlands will have a completely free price economy with two major exceptions, (1) house rents will probably remain controlled for a long time to come, (2) minimum prices for certain agricultural products, especially milk, will continue. The total amount of subsidies paid in Belgium to the lower classes and in support of the low grade coal mines, of gas, and of railways is even now larger than the total amount of the subsidies granted in The Netherlands, mainly to agricultural producers.

Before the War the hourly wage-level in Holland was nearly 60% higher than in Belgium. In March, 1949, the hourly wage-level in Belgium had become 27% higher than in Holland.

The full repercussions of the devaluation of sterling and of the guilder announced in September, 1949, upon conditions in Benelux remain to be seen. We cannot yet speak positively but some authorities argue that the fact that The Netherlands

have devalued the guilder by 30·5%—thus keeping pace with sterling—while Belgium has only devalued the franc by 12·3% should help the cause of economic union between the two countries. This differential devaluation will, admittedly, increase the margin which separates prices and wages in the two countries; but they consider this is a margin which should be widened if the chronically creditor position of Belgium *vis-à-vis* The Netherlands is to be corrected, since the lack of equilibrium in the balance of payments between the two countries is one of the real obstacles to the fusion of their economies. Anything which helps to remove that obstacle, and thus leads to the free inter-convertibility of their currencies, is a direct contribution to their complete economic union. Some, indeed, even maintain that it may ultimately favour the equalization of wages in the ports of Antwerp and Rotterdam.

In August, 1949, it was computed that the volume of money in The Netherlands had not risen very much more since 1938 than the price level had. There are, of course, several ways of calculating the relation of the total money volume and the price level compared with pre-war levels, but some observers argue that the most realistic figures indicate that in August, 1949, the Dutch money volume was only some 10 per cent. higher than it should be according to pre-war standards. However this may be, the relevant data on which to form a judgement are summarized below and in the charts on page 69:—

INDEX FIGURES
1938 = 100

	Belgium	1949	*Holland*	
Total Money Supply	373	May	283	May
(Inc. Blocked Deposits)	462		308	
Wholesale Prices	362	May	288	May
Cost of Living	363[1]	March	219	March
Industrial Production	118	April	120	April
Discount Rate	3½%	June	2½%	June
Government Bond Yield	4·62%	June	3·12%	June

[1] Retail Prices.

SOURCE: I.M.F. International Financial Statistics, 1949.

Some comparative figures, extracted from *The Economic Bulletin for Europe* and recently published by the United Nations' Economic Commission for Europe, are, perhaps,

enlightening. It will be observed that the index for The Netherlands already was on a par with that of Belgium. But these figures do not show the hourly productivity per worker, and that, as Professor Robbins underscores on an earlier page of this *Review*, is what chiefly matters in the context of events.

Indices of Industrial Production

First Quarter of 1949, as Percentage of 1938

Belgium	122	Netherlands	122
Denmark	135	Norway	130
France	124	Sweden	147
Italy	90	United Kingdom	131

The trade policy of Benelux is to be based on a joint monetary fund to be formed by the three member States. The Belgium-Luxemburg side has, however, made it known that it is desired to keep the substantial gold holding of the B.L.E.U. (Belgium–Luxemburg Economic Union) outside this joint arrangement. On any long-headed calculation of chances this seems regrettable. Benelux with limited reserves at its disposal for the joint trade policy will have to behave in a very different manner from a Union possessing substantial resources. Francis Bacon was right when saying:

> In civil business, what first? Boldness. What second and third? Boldness.

If each party insists upon doing the things which the other is peculiarly fitted to perform the principle of a real division of labour, which is one prime object of Benelux, will be thrown to the winds. The Belgian insistence on a limitation of the import of Dutch vegetables should the price fall below a certain level, and any Dutch determination to develop heavy industry on a very extensive scale, would seem difficult to justify. The Dutch have long excelled in light industries and there would seem to be scope here for further expansion. They are, however, confronted with special problems in view of the very rapid increase of population in The Netherlands. These will, of course, ultimately be influenced by the peaceful development of Western Germany, which all must desire, and by the trend of events in regard to Indonesia.

IV. The Difficulties

First a word in regard to a point already touched—the difference of temperament of which Belgians and Dutch are themselves supremely conscious. It enters into every sphere of their activity as into all their faculties. Indeed both nations have, perhaps in superabundant measure, the sense of historical continuity looking backwards to the past and reaching forward to the future. The Belgian is first and foremost an individualist and a liberal in the widest sense of the term; the Dutchman has a passion for strong and just administration and his art of treasury control has long made the Dutch Exchequer a marvel of efficiency. The Belgian's attachment to liberty and the Dutch belief in co-ordination are characteristic social growths which are as much adapted to their respective countries as the lichen to the rock on which it grows. They strike the observer at every turn. Take but a single example, agriculture: in The Netherlands it is controlled at every stage, and with eminent success, by corporative bodies; in Belgian agriculture more is left to individual initiative. Everything has obvious roots in past history; and, perhaps, in a land won from the sea it was a matter of transcendent importance to combine, while in a country which suffered from centuries of foreign domination it is only natural that there should now be the freest economy in Europe.

In the case of the Dutch, as of the English, the sense of national unity was evolved in the great struggle with Habsburg Spain.

It was otherwise with the Belgians, both Flemings and Walloons, for all Europe has sought at one period or another to exploit them by a dominance which too often darkened into oppression. Thus most of the costly wars and distant expeditions of Charles V, wherein they seldom had any direct concern, were financed not with silver from the mines of America but with the wealth of The Low Countries, in other words with the revenues of Antwerp, of Bruges, and of Ghent, no matter whether His Majesty carried on his wars and expeditions as King of Spain or as Emperor of Germany. "These," wrote the Venetian Ambassador, Michele Soriano, from Madrid in 1559, "these are the real treasures of the King of Spain, these are the rich mines, these the 'Indies' which for so many years

have sustained the enterprises of the Emperor." [1] Thus again, when the Southern Netherlands (Belgium) had become a dangerous zone for the Dutch during and after the ascendancy of Louis XIV, Dr. G. M. Trevelyan tells us that the so-called Dutch Barrier became "the hinge of European diplomacy." Under this scheme, which was a variant of the buffer-state system, the Dutch were allowed to hold certain towns garrisoned with their own troops who were maintained there at the expense of the surrounding Belgian populations; but the Barrier was far from being merely a buttress of defence against France since it enabled the Dutch for many a long decade to keep the Belgians in a state of economic weakness which prevented them from becoming dangerous competitors in trade. Thus again, in the reign of George I, Sir Robert Walpole strongly and successfully opposed the nascent Ostend Company which had been projected partly as the resultant of the earnest desire of the Southern Netherlands to regain their old participation in the Indian trade, dating back to a time prior to the discovery of the Cape route. These illustrations might easily be multiplied.

The upshot of this secular economic thraldom was that the Belgians acquired the habit of mistrusting official regulations and controls because so often, and for so long, they were oppressive and covered measures harmful to their own interests. Thus a propensity to disregard regulations and evade direct taxation gathered strength with the years and was almost sublimated into a form of patriotism. Among Belgians a deep-seated lack of confidence towards all governing authorities entered into their very bones and persisted even after the triumph of Belgian Independence which, after all, was only attained little more than a century ago. The Belgian is still suspicious and resentful of all authority which interferes with his economic freedom. Indirect taxation in Belgium to this day yields 60% of the total, direct taxation 40%. In The Netherlands the converse applies.

We have stressed the psychological factor, perhaps with somewhat wearisome ingemination, because, as Bismarck rightly opined, imponderables cannot safely be overlooked.

It requires no great discernment to detect that the conjuncture of circumstances which resulted in The Netherlands

[1] Alberi, E.: *Le Relazioni degli Ambasciatori Veneti al Senato*, Serie i, Vol. III, p. 357.

only being cleared of the enemy some 8 months after the liberation of Belgium was bound to add to the difficulties of inaugurating Benelux, since delay not only intensified existing difficulties, but created fresh ones. It is easy on a retrospect to assert that many of the troubles which have arisen would have been avoided if only the merger had been imposed on the member States immediately after the statesmen in London had reached agreement in September, 1944. Even if we assume, what, of course, requires a great deal of prior investigation, that this analysis is correct, the point is now of purely academic concern since the logic of events made it impossible to do what has now been suggested should have been done.

Belgium as all the world knows was liberated in a matter of days and escaped with her industrial equipment almost unscathed. She was thus able to seize the passing opportunity, which she did with such brilliant success, afforded by the economic agony of the Ruhr to supply to her Allies in a sellers' market the steel they so sorely needed. She had ended the War with considerable dollar reserves which her sales of steel to a certain extent augmented; for many months she was a base for the large Allied armies operating in Germany, and thus again she was able to increase her foreign currency reserve, all of which served her in good stead during the next two critical years. Nor was the Congo a burden to any appreciable degree upon the manpower or the monetary resources of the Parent State. Having put into operation a drastic financial measure known as the *Plan Gutt* so as to maintain a relation between the volume of currency and credit outstanding and the volume of goods on which it could be expended, she proceeded to buy raw materials from the Western Hemisphere and both capital and consumer goods from The United States. Abundance, as contrasted with controlled austerity, was a matter of deliberate policy. Of set purpose the shops were saturated with goods so as to stimulate domestic output, and wages and prices were allowed to rise with comparatively little restriction. Controls and rationing were minimized, reliance was placed on the price mechanism, on private enterprise and initiative and, above all, on very hard work of one and all to restore the economy of the country. To outward seeming, private saving has not been much in evidence and there has been a high rate of consumption, perhaps at some expense to

long-term prospects. The Belgian Ministry of Economic Co-ordination has warned that " the economic system of the country has aged, and this ageing results in an increase in sales prices which constitutes an inevitable menace for the future." However this may be, and it is a matter which has given rise to keen and copious contention among Belgians themselves, one cannot but be struck by the vigour and vitality that Belgium has revealed in her reconstruction. The Belgian's cleverness, his vivacity, his unaffected zeal, his gay fancy always seeing the light side of everything, his imperturbable good humour and buoyant elasticity of spirits—all these qualities have contributed to the crowning result.

> Every British visitor to Belgium, wrote Mr. Paul Bareau, in LLOYDS BANK REVIEW of January, 1947, has been struck by the enthusiasm, the will to work, the readiness to serve and to please that are to be found in that country. The pace at which rebuilding has progressed in devastated towns such as Antwerp and Liége should be an example to Britain. There are no restrictions on the number of bricks which a Belgian building operative is allowed to lay in one day.

With the important reservations of the transport system and housing, Belgium was not burdened to the same extent as her neighbours with major problems of physical reconstruction or of overcoming wartime losses of foreign assets. Furthermore she has not suffered in anything like the same degree as Holland from the economic prostration of Germany. Indeed, the slow agony of the Ruhr and the world shortage of steel together secured a strong and lucrative market for Belgian and Luxemburg mills and their production expanded as French or Swedish iron ore and American fuel became available. The Belgians themselves are the first to admit these advantages and have been quick to seize or create opportunities. They held, and perhaps in some considerable measure rightly so, that it was vital to encourage production in such exceptional conditions (even if it involved the postponement of some other needs) by offering every incentive to employers and workers, and on this, among other grounds, as has been noted already, they deliberately saturated the country with consumer goods at some sacrifice of capital expenditure.

The traditional trade of Belgium in pre-war days was

mainly based on the import of raw materials and foodstuffs from the Western Hemisphere and on the export of steel, manufactures, and some produce to Western Europe and other regions, and this trade was, as is well known, financed very largely through the conversion of sterling into dollars. After the War, owing to inability of European countries to pay for Belgian exports in anything but soft currencies, a sharp contraction of trade was feared, and that at a time when scarce goods such as steel were in maximum demand for European economic recovery upon which the U.S.A. are set for major reasons of policy. Accordingly arrangements have been made, and are supervised by ECA (the Economic Co-operation Administration), whereby Belgium, in return for supplying goods to other European countries for soft currency, is able to secure an equivalent sum in dollars with which to pay for her own imports from dollar areas. The heart of the problem is, of course, how long and what then, and will it be possible to attain an economic balance before such aid terminates, as some day terminate it must? On the whole we see no real grounds for pessimism. Even in a buyers' market, in the first six months of 1949, Belgian exports have been maintained at a high level.

When we turn from Belgium to The Netherlands the picture is far more sombre yet it is lightened by the extraordinary speed with which the devastation wrought by the War is being repaired. Never have the old virtues of simplicity and discipline, of honest toil and pecuniary integrity, stood a country in better stead. The aim of the Government has been to canalize and direct the manifold energies of the people into long-range objectives. The recovery, only made possible by the generous aid which The United States are giving to the reconstruction of Europe, has still very far to go, but its foundation is a vivid perception of realities and a masculine grasp of facts by the Dutch themselves. The Dutch mercantile marine, apart from tankers, is now above the pre-war tonnage; the restoration of the railways makes a remarkable impression; production levels are above pre-war figures; moreover, despite the need for substantial imports for repairs and developments, improvement in the large balance of payments deficit on current account as against 1947 has already been made possible by a marked increase in exports during 1948.

The Netherlands became the battle-ground of some of the

bitterest fighting of 1944 and 1945 and thousands of British and Americans laid down their lives in the liberation. Dykes were breached by the Germans, fertile areas were inundated by the sea, damage to the railways, much of it purely malicious, is computed at over $200 millions at pre-war prices, industrial plant suffered enormous destruction and the populations behind the fighting line were reduced to starvation. It is, indeed, almost impossible to exaggerate the miseries which the Dutch were compelled to endure. The wanton bombardment of Rotterdam in 1940 was only the first stage in a swift series of accumulating disasters. The Netherlands suffered losses amounting to nearly one-third of the national wealth during the German occupation. And when at last peace came misfortune followed misfortune. It is against this dark background that the Dutch Government had to decide upon a policy.

> It is obvious, the ECA report sums up, that because of staggering wartime losses and because of the need for developing new sources of revenue the Dutch must carry out a substantial capital formation drive. The fact that they have been willing to restrict consumption to relatively low levels suggests the importance they themselves place on capital expansion.

The disruption of the German economy was bound to react severely on the Dutch. Ever since the Thirty Years' War they had played a large part in the German river traffic, and in 1939 50% of the Rhine barges were Dutch, and 15% Belgian. Now such traffic as remains passes largely through Bremen. The industrial basin of Western Europe forms the natural hinterland of The Low Countries, and the Ruhr had been the traditional market for Dutch vegetables. Moreover the Dutch had large capital investments in Germany which were wiped out at a stroke.

V. Conclusion

Indeed to all humane observers the central problem of Germany presents a terrible dilemma which looms large when her way of life is uncertain, her soul is in a ferment and ambition thicksighted. On the one hand she is the economic and geographical core of Europe and without a prosperous Germany all

Western Europe, notably The Low Countries, will lack animation, many knotty political issues will fail to be cleared up, and the Fatherland will again become a seedbed for those obscure stresses and instincts which work below the threshold of rational life and often surprise the reason by the energy and vehemence of their appeal. On the other hand Germany has twice within a lifetime played high for victory and lost the stakes, nor can anyone with an eye in his head be blind to the danger of a resurgence of militarism among a people who sometimes seem singularly ungifted for politics. If peace again trembles in the balance, and interest and impulse do not coincide, will Germany's leaders be on the side of intelligent solutions, or will the doctrine of Heinrich von Treitschke again prove the master element? Let nobody belittle the horns of this dilemma which confronts Germany and her neighbours. The principal hope and promise for humanity, even the pacific handling of the Scythian menace, most certainly the abiding welfare of The Low Countries, lie in its wise resolution. Thanks to the North Atlantic Treaty we may now have a greater confidence, the more so because that instrument does not rest on necessary force alone; it is also based on an attempt to understand the general complex of international relations and the great and inspiring features of alien civilizations. It is only thus security will prove enduring, so that the palaver may end and the work of statesmanship at last begin. There has, perhaps, at times been want of alacrity and of power of action on our part in confronting the internal problem since 1945; difficulties were stupendous, yet not all that went awry was merely the logical sequel of Potsdam.

> But, in spite of all the criticizing elves,
> Those who would make us feel, must feel themselves.

What exactly in this grim present world is now the role of the Angel of Light? Is it "high fantastical" that Benelux might afford the true answer as the archetype of an international union of wider compass wherein Germany may find a real as distinct from a mechanical pacification? Never has there been greater need for a forward-looking policy, alike prompt and well-grounded in knowledge. Without some larger economic framework the German problem is seemingly insoluble, without

this the German problem is too gigantic in its bearings, too complex in the mass of its detail, to be cleared up.

If there is no gainsaying the fact that a peaceful and a prosperous Germany is of decisive significance to The Low Countries, in any appreciation of the causes which have led to delay in the negotiation of Benelux the consequences of the Japanese occupation of Indonesia, where the Dutch have performed a great office in developing the economy of a vast miscellany of races, are of major importance. It is no part of our plan to discuss the Indonesian question which abounds in delicate issues. Others have spoken on the whole subject with precision at Chatham House and *The Economist* has devoted various articles to it.[1] Our purpose is humbler and more practical; it is to insist upon the need of an agreed and early settlement, so vital for the enduring interests of Indonesia and The Netherlands and for the revival of multilateral trade. In the ECA Netherlands Country Study dated February, 1949, we read:

> Wholly aside from the ultimate disposition of the Indonesian problem, its economic recovery would represent a major contribution to a viable Europe. Not only has Indonesia been historically an important supplier of critical raw materials but because of a normal dollar surplus with the Western Hemisphere it has been an important source of dollars for Europe. Without the restoration of Indonesian trade, The Netherlands difficulties in regaining economic stability will be seriously increased. A modest programme of economic aid to Indonesia, whenever it could be appropriately extended, might therefore make a direct contribution to European recovery at least as large, dollar for dollar, as any other use of ECA funds. . . . The importance of The Netherlands as a factor in the achievement of our aims and objectives in Europe, its alliances (the Benelux

[1] Dr. van Mook's address at Chatham House, together with a summary of the subsequent discussion in which Lord Wavell and others took part, will be found in *International Affairs* for July, 1949. See also an article in *The Economist* of June 18th, 1949. The English reader may consult a useful brochure of statistics on The Netherlands and Indonesia published by the Foundation of Statistics at Leyden in May, 1947.

Union and the Brussels Pact), and the long history of cordial United States—Netherlands relations makes this aid vital to the maintenance of the structure of European democracy.

How narrow is the margin which divides civilization from chaos has been made alarmingly clear by the experience of two World Wars and their train of ensuing evils. Once again, heavy banks of cloud hang with occasional breaks of brighter sky over Europe and the world. The leaden inhibitions of thought which are ice-bound in the totalitarian ethos threaten that high standard of life and achievement which was only reached after long centuries of evolution by the discipline and imaginative genius of generations of the more gifted peoples of Europe. Between a political philosophy rooted in the Christian tradition of pity and love and the Communist system spurning such ideas as the sense of evidence, the rights of man, and parliamentary debate, there can be no compromise.

Nor, indeed, is there any question more pertinent to the future welfare of mankind than how to secure that international equilibrium which alone is capable of placing an insuperable hindrance in the pathway of demagogic imperialism. " For you know, and we know," writes Thucydides in the *Melian Dialogue*, " that right is considered, in men's discussions, only when both parties are of equal power ; but the strong do what they can, and the weak have to submit." Upon the true solution of this problem of equilibrium, only to be achieved at the cost of eternal vigilance and in continual survey of broad social facts, depends the avoidance of further bloodshed, so that we may pursue our common interests. Then we may realize that aspiration after order and harmony which man is always pleased to entertain and his perversity so often tends to frustrate.

The announcement of devaluation of sterling in September, 1949, may ultimately, as already suggested, ease the situation, especially as Belgians and Dutch share the old and salutary belief that it is the duty of every worker to give to his work the best that is in him. Benelux, if soundly conceived and securely

laid in a basis of convertibility of currencies and a real division of labour, may yet become the prototype of a working as distinct from a theoretical fusion of interests—the latter a field where we have too often witnessed the risks that are run, and the suffering which emerges, through not first thinking things out. Thanks to the generous and far-sighted co-operation of the United States, Benelux may unite the opportunity for practical improvements in government with broad and glowing sympathies with the needs and elemental instincts of mankind. We can, indeed, hardly imagine a finer or more inspiring task for statesmen, nor a more noble ambition than that it should bear the mark of their constructive hand.

And so we see no grounds for despondency, but rather a reason for greater confidence, in the delays which have recently supervened in bringing Benelux to fruition. Indeed, when we are concerned with the temple of conciliation and peace, above all with stubborn problems of currency and a vast project of administrative reorganization, it is, perhaps, pertinent to recall that the biographer of Sir Robert Peel—*nomen intra has ædes semper venerandum*—reminds us that:

> It was peculiar to him that, in great things as in small, all the difficulties first occurred to him; that he would anxiously consider them, pause, and warn against rash resolutions; but having convinced himself after a long and careful investigation not only that a step was right to be taken, but of the practical mode also of safely taking it, it became a necessity and a duty to him to take it. All his caution and apparent timidity changed into courage and power of action, and at the same time readiness cheerfully to make any personal sacrifice which its execution might rightly demand.

ALWYN PARKER.

September 19*th*, 1949.

Statistics: Explanatory Notes

Marshall Aid.—On September 29th Congress approved an amount of \$3,628·4 millions for European aid for the year July, 1949, to June, 1950. This is, however, nearly \$150 millions less than the total of \$3,776·5 millions taken as a basis for the allocation of aid among recipient countries at the end of August, by Baron Snoy and M. Marjolin of O.E.E.C.—as given, for the five main countries, in the table below. This fact will presumably now make necessary the revision of the 1949/50 division of aid together with a reconsideration of the intra-European payments scheme in the light of the situation resulting from devaluation.

	1949/50				1948/49	
	Direct Marsh-all Aid \$m	Plus net receipts or minus net contributions under Intra-European Payments Scheme \$m	Net Aid \$m	% of Euro-pean Total	Net Aid \$m	% of Euro-pean Total
U.K.	962·0	–69·0	893·0	*23·6*	957·0	*20·1*
France	704·0	+223·6	927·6	*24·6*	1304·2	*27·4*
Italy	407·0	–24·5	382·5	*10·1*	535·2	*11·3*
Belgium / Luxemburg ..	312·5	–400·0	–87·5*	—	40·4	*0·9*
Netherlands ..	309·2	+136·2	445·4	*11·8*	541·3	*11·4*

* Representing long-term credits to the U.K., France and Netherlands.

Devaluation.—The chart on page 58 shows the changes in value of some important foreign currencies, in terms of pence per unit, during the three most recent periods of widespread adjustments in exchange rates. Since September 19th last the sterling value of the U.S. dollar has been increased by 44 per cent. It is now just over 7/–, compared with 5/– before devaluation and about 4/– prior to our departure from gold in 1931. The Canadian dollar is now at a 10 per cent. discount in relation to the U.S. dollar and is thus worth slightly less in terms of sterling. The value of the French franc in sterling shows a successive fall; in the months after September, 1931, it averaged 2½d. but by the outbreak of War had already lost half its value in terms of sterling. Since September 19th it has been worth about a farthing, representing a slight increase, in fact, on its previous value.

The American Recession.—The relative mildness of the recession in American business activity is brought out by the charts on page 59. Industrial production, after a fall of 17 per cent. in the eight months from last November, recovered for the first time in August—to a level, it should be noted, nearly 70 per cent. above the pre-war average. Personal income shows only a modest decline whilst new construc-

tion, as a whole, appears to have been almost unaffected. Bank loans, in contrast, fell by over two thousand million dollars in the first six months of 1949.

The Dollar Gap.—By the end of September our gold and dollar reserves had fallen to £351 millions, reckoned at the old rate of exchange. This represents a recovery of some £20 millions from the lowest point touched on the eve of devaluation, but even so means a loss of £55 millions during the quarter, following one of £65 millions in the second quarter. From the second and third charts on page 60 it will be seen that very little progress in the expansion of exports to the Western Hemisphere had been made prior to devaluation. Shipments to the U.S.A. and Canada in the second quarter of 1949 were less than 7 per cent. of total exports, in contrast to 9 per cent. in the first quarter of 1948.

The Export Drive.—From the first chart on page 61 it will be seen that the trend of exports since February has been slightly downwards after an almost continuous rise during the last three years. In volume the decline has been even sharper and, on a working day basis, exports fell in August to 138 per cent. of the pre-war level—the lowest figure since October, 1948, and a fall of 15 per cent. from the December peak of 162. Imports, in contrast, have tended to increase and in June exceeded £200 millions. As a result the import surplus rose in the second quarter to £137 millions, against £64 millions in the first three months of the year.

Security Yields.—Over the last three years two periods stand out when security yields rose abruptly. The first, during the summer of 1947, culminating in the August convertibility crisis; and the second in the three months this year prior to devaluation. In the latter period, however, the rise in yields was much more precipitous. As a result the market no longer regards War Loan 3½ per cent. as likely to be redeemed in 1952 and the yield on that stock is, in fact, higher than on irredeemable old Consols.

The Tourist Industry.—Nearly half a million tourists from abroad visited this country during 1948 and it is expected that the 1949 total will be still higher. Together with visitors in transit, their expenditure amounted to £33 millions, excluding fares paid to shipping and airline companies, and of this over a third was spent by tourists from the dollar area. Total receipts from American visitors were greater, in fact, than the earnings of any single U.K. industrial export to the U.S.A. It is not sufficiently realized how much a sustained improvement in transport and hotel services, greater cleanliness in retail food shops, and a speed-up in long distance telephone calls would promote an influx of overseas visitors.

European Trade.—Two factors of particular importance in European trade are brought out by the charts on page 64. First, the decline in intra-European trade compared with the shift towards overseas markets; although intra-European trade has gradually increased since 1946 it was still 30 per cent. less in volume last year than in 1938, whereas trade with the outside world, in both directions, was fully back to the pre-war level. Secondly, it can be seen that the recovery in European exports has been very largely due to the expansion in U.K. exports. Including the U.K., total European exports last year were 82 per cent. of the pre-war volume whereas, if the U.K. is excluded, the figure would be only 67 per cent.

East-West Trade.—The chart on page 65 shows that trade across the Iron Curtain before the War was far more important to the East than to the West, taken as a whole. In 1938, for example, nearly three-quarters of total Eastern European

exports were taken by Western Europe, although this accounted for less than a tenth of total Western *imports*. Since the War this trade has declined and last year, in volume, was less than half the pre-war level. The expansion in East to West trade during 1948, however, was sufficient to restore the traditional surplus in favour of Eastern Europe, particularly in trade with the U.K.—the best customer for East European exports and the most important source of supply.

Petroleum.—In the ten years to 1948 world output of petroleum increased by nearly three-quarters. Although the U.S.A. remains the leading producer, the proportion accounted for by the Middle East rose from 6 per cent. in 1938 to double that figure in 1948. Consumption also has increased in America; last year it was almost twice the pre-war figure, in contrast to only a small rise in this country. At the present rate of consumption, known oil reserves, at the end of 1948, would last about another 23 years.

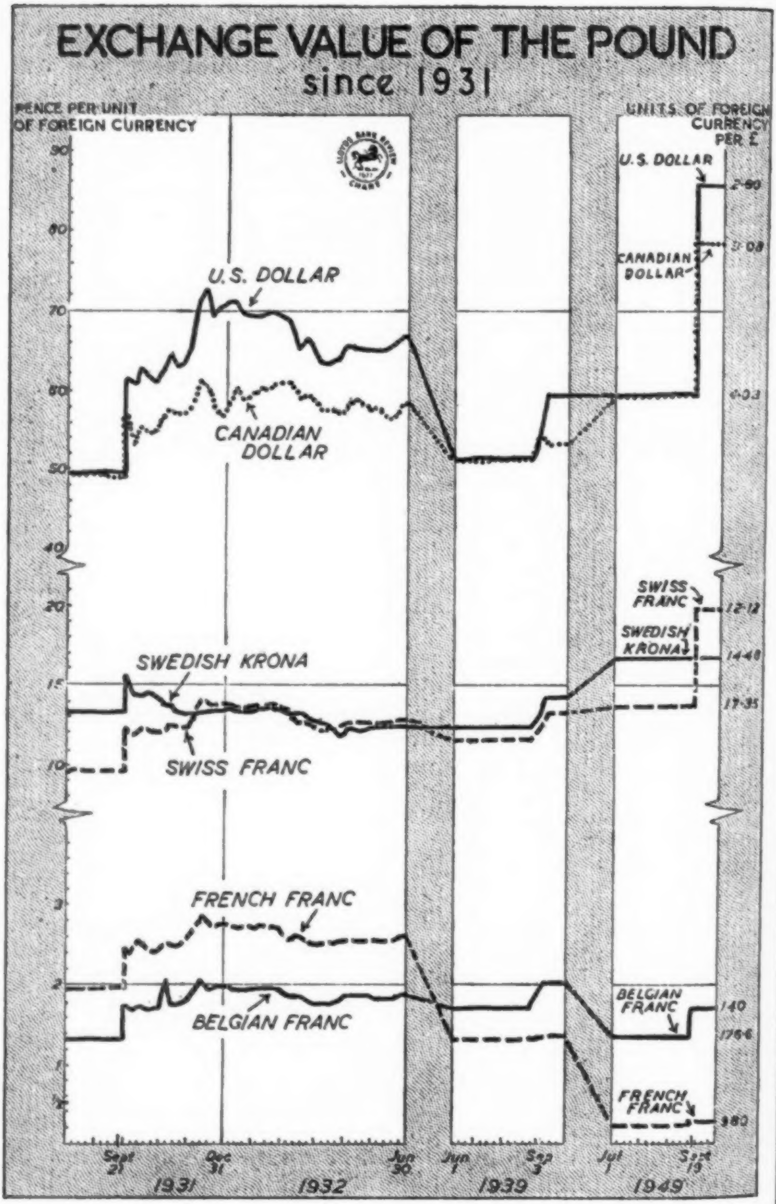
Benelux.—In connection with the article on "Benelux" by the Editor in this issue of the REVIEW we give, on pages 67 to 69 charts and tables illustrating recent economic developments. The reader is also referred to the July, 1949, issue in which, on pages 44 and 45, charts were given depicting current trends in Belgium.

As a participant in world trade (first table, page 67) the three Benelux countries now rank third, accounting last year for 6 per cent. of world exports and 7 per cent. of world imports. There is a great difference, however, between the trading positions of Belgium/Luxemburg and The Netherlands, as shown by the second table. In 1948 the import surplus of The Netherlands was equivalent to $700 millions, over five times that of Belgium.

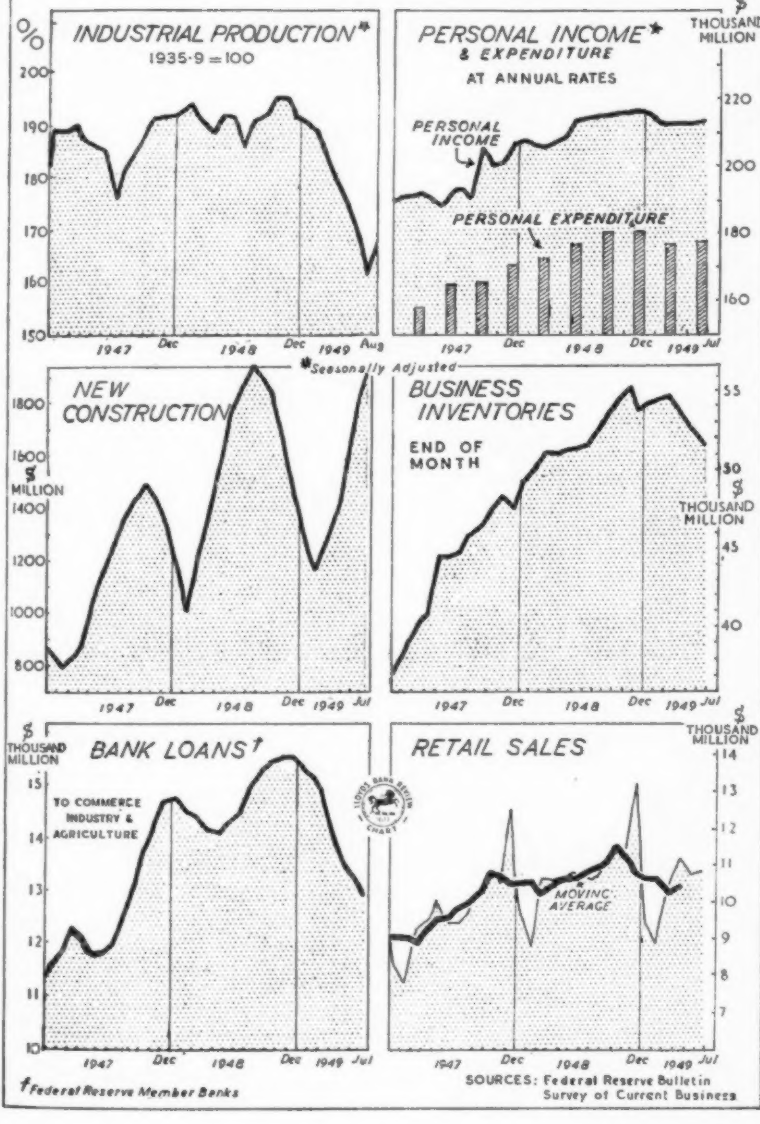
As regards The Netherlands (page 68) there had been by the spring little change, on balance, in the level of industrial production since the end of last year. Shipping under construction is now higher than before the War, although at the end of June it represented only 7 per cent. of world tonnage under construction, compared with 10 per cent. in 1938.

Indonesia.—Before the War, in prosperous years, about 15 per cent. of the Dutch national income was dependent on Indonesia. In 1947, however, this had been reduced to only 5 or 6 per cent. Some of the main trends in the Indonesian economy are depicted in the charts on pages 70 and 71. Population has steadily increased and has risen by nearly a half since 1920. Of the working population, at the occupational census in 1930, 70 per cent. were engaged in the production of raw materials and foodstuffs. Production of tin and rubber last year was above the pre-war level and, taken together, exports of these two products accounted for more than a third of total exports. A large part of Indonesia's external trade is naturally with The Netherlands, which in 1948 took 36 per cent. of her exports and provided 19 per cent. of her imports—a figure exceeded, however, by the U.S.A., with 22 per cent.

Textile Exports.—Before the First World War textiles accounted for over a third of the value of U.K. exports. After touching a peak in 1918 of nearly 50 per cent. there was a steady decline in the percentage figure from the mid 'twenties until 1938. The rise in the proportion up to 1942 was due, not to an increase in textile exports (see first chart page 72) but to a decline in exports of *other* commodities. Since then the down-trend has been resumed, although there was a slight recovery —to 18 per cent.—last year.

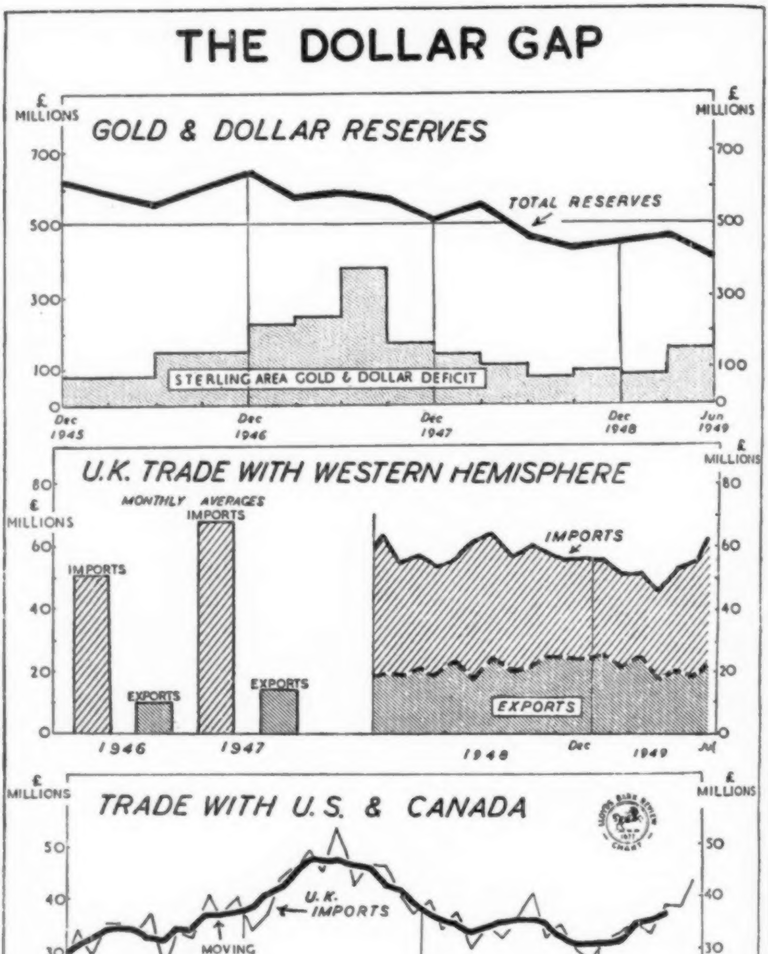

EXCHANGE VALUE OF THE POUND
since 1931
PENCE PER UNIT OF FOREIGN CURRENCY
UNITS OF FOREIGN CURRENCY PER £
U.S. DOLLAR
CANADIAN DOLLAR
SWEDISH KRONA
SWISS FRANC
FRENCH FRANC
BELGIAN FRANC
2·80
3·08
4·03
12·12
14·40
17·35
140
176·6
980
Sept 21
Dec 31
Jun 30
Jun 1
Sep 3
Jul 1
Sept 19
1931
1932
1939
1949

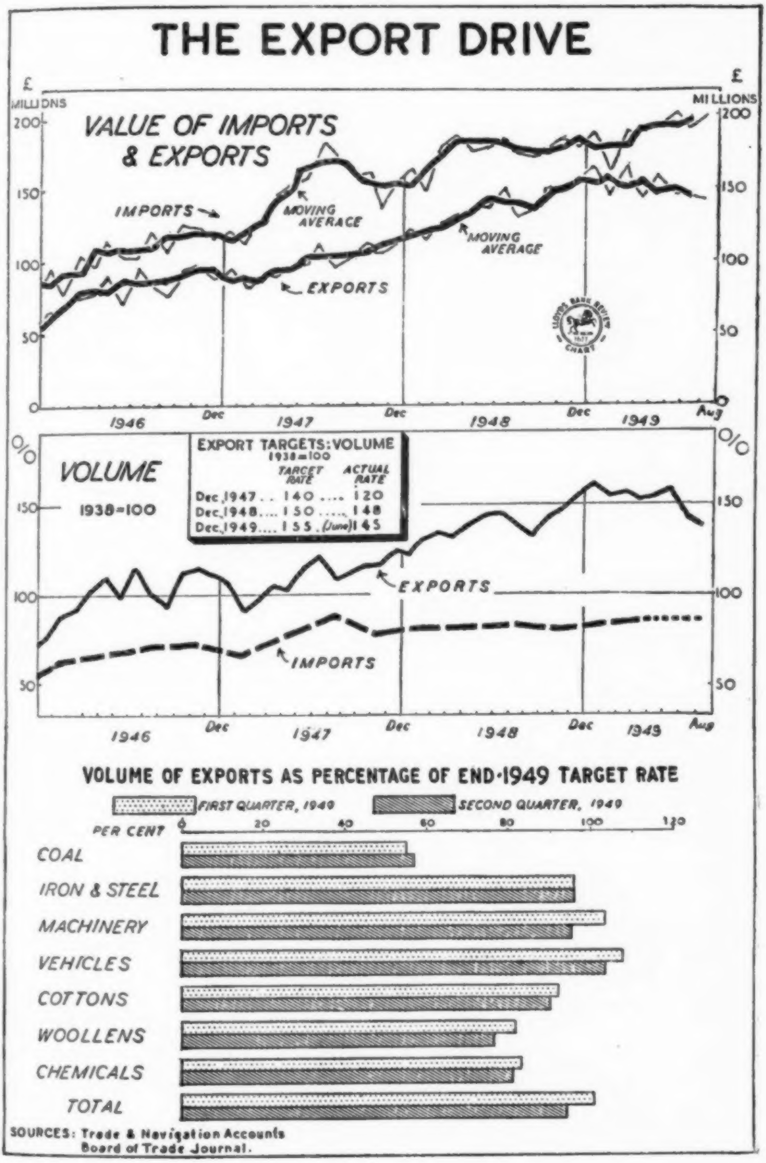
THE AMERICAN RECESSION

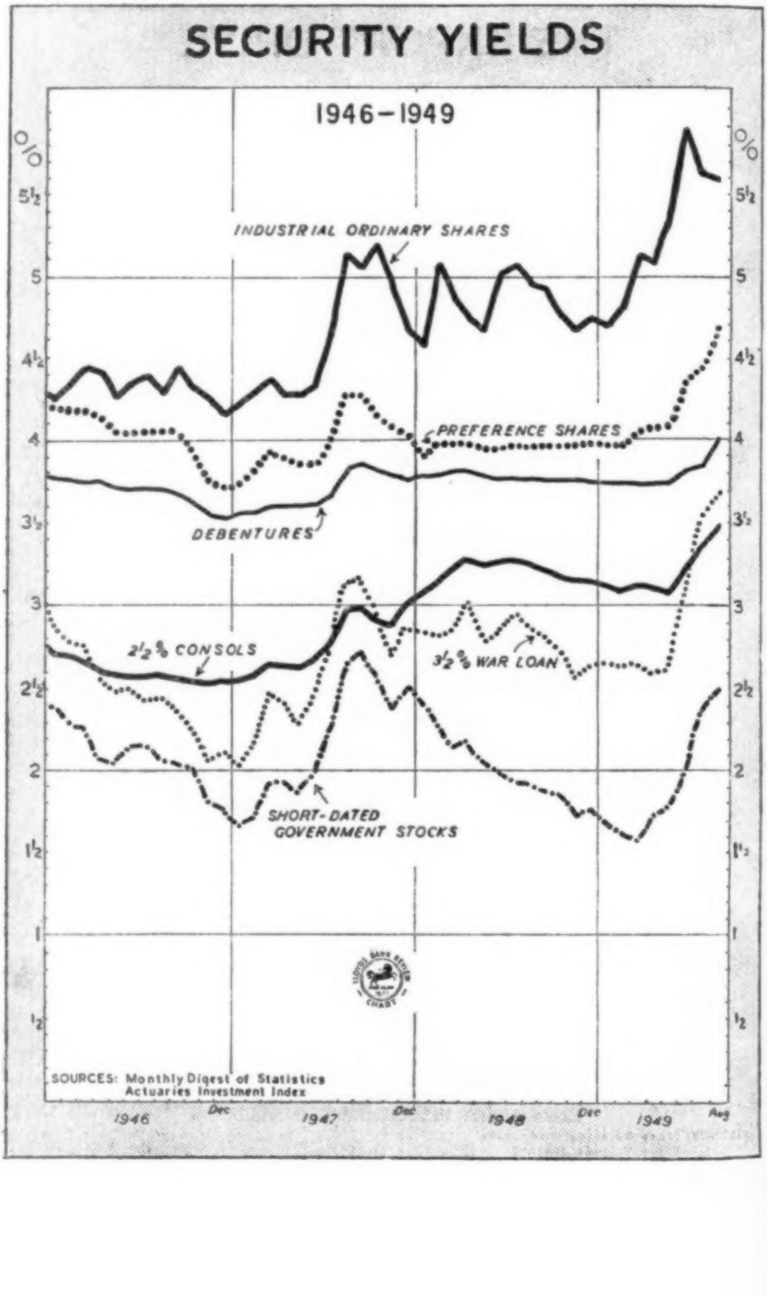


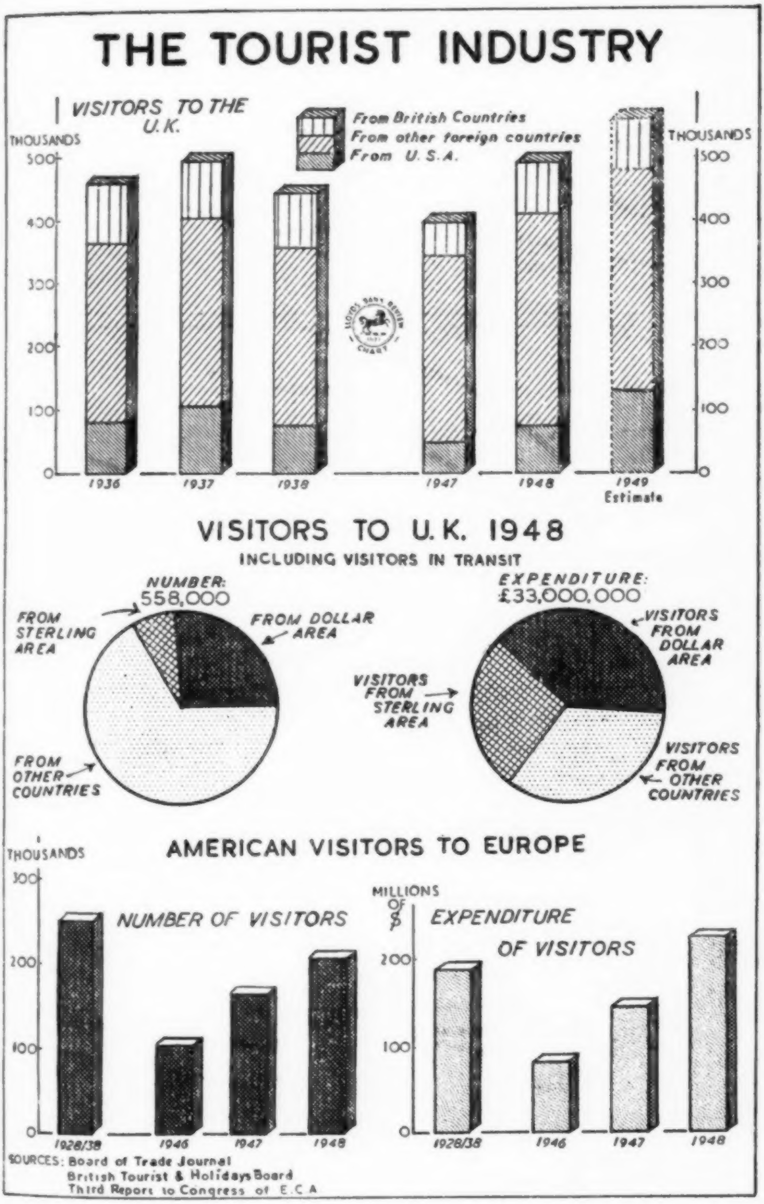
† Federal Reserve Member Banks

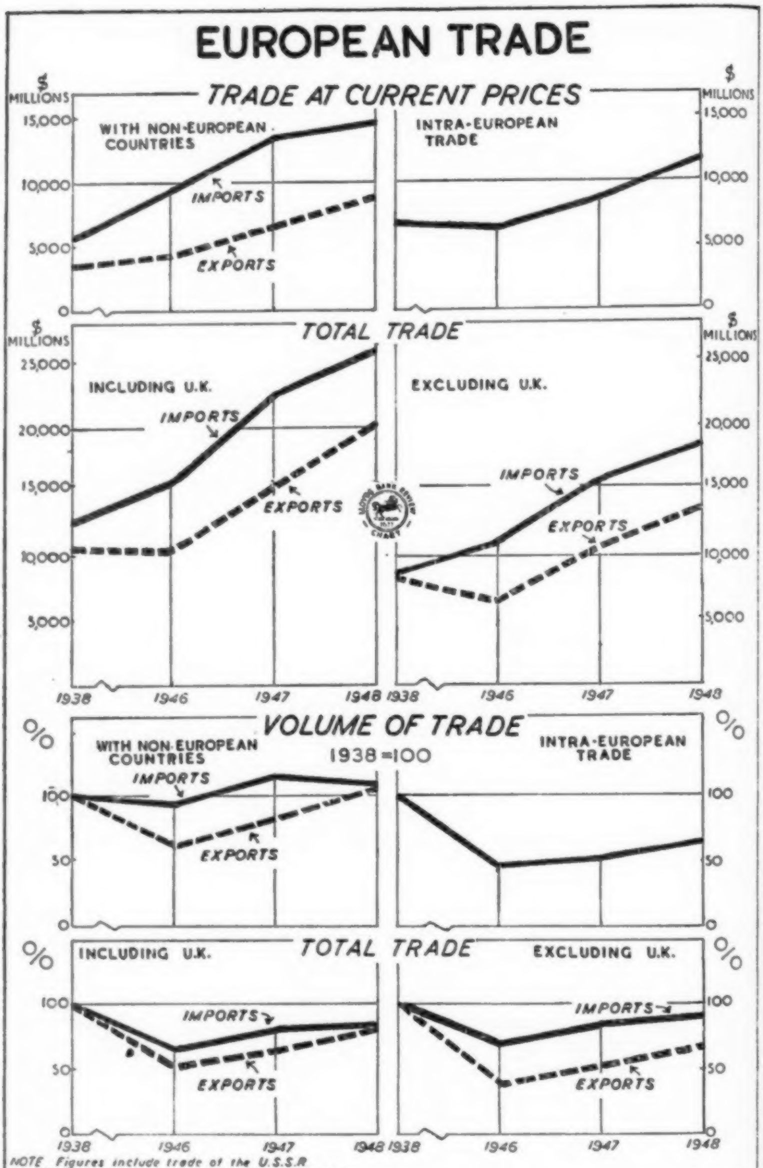
SOURCES: Federal Reserve Bulletin
Survey of Current Business


THE DOLLAR GAP
GOLD & DOLLAR RESERVES
£ MILLIONS
TOTAL RESERVES
STERLING AREA GOLD & DOLLAR DEFICIT
Dec 1945
Dec 1946
Dec 1947
Dec 1948
Jun 1949
U.K. TRADE WITH WESTERN HEMISPHERE
MONTHLY AVERAGES
IMPORTS
EXPORTS
1946
1947
1948
Dec
1949
Jul
TRADE WITH U.S. & CANADA
U.K. IMPORTS
MOVING AVERAGE
U.K. EXPORTS
SOURCES: Balance of Payments White Papers
Trade & Navigation Accounts.


THE EXPORT DRIVE
£ MILLIONS
VALUE OF IMPORTS & EXPORTS
IMPORTS
MOVING AVERAGE
MOVING AVERAGE
EXPORTS
1946
Dec
1947
Dec
1948
Dec
1949
Aug
%
VOLUME
1938=100
EXPORT TARGETS: VOLUME
1938=100
TARGET RATE ACTUAL RATE
Dec. 1947 .. 140 120
Dec. 1948 .... 150 148
Dec. 1949 .... 155 . (June) 145
EXPORTS
IMPORTS
VOLUME OF EXPORTS AS PERCENTAGE OF END-1949 TARGET RATE
FIRST QUARTER, 1949
SECOND QUARTER, 1949
PER CENT
COAL
IRON & STEEL
MACHINERY
VEHICLES
COTTONS
WOOLLENS
CHEMICALS
TOTAL
SOURCES: Trade & Navigation Accounts
Board of Trade Journal.


SECURITY YIELDS
1946–1949
%
5½
5
4½
4
3½
3
2½
2
1½
1
½
INDUSTRIAL ORDINARY SHARES
PREFERENCE SHARES
DEBENTURES
2½% CONSOLS
3½% WAR LOAN
SHORT-DATED GOVERNMENT STOCKS
SOURCES: Monthly Digest of Statistics
Actuaries Investment Index
1946
Dec
1947
Dec
1948
Dec
1949
Aug

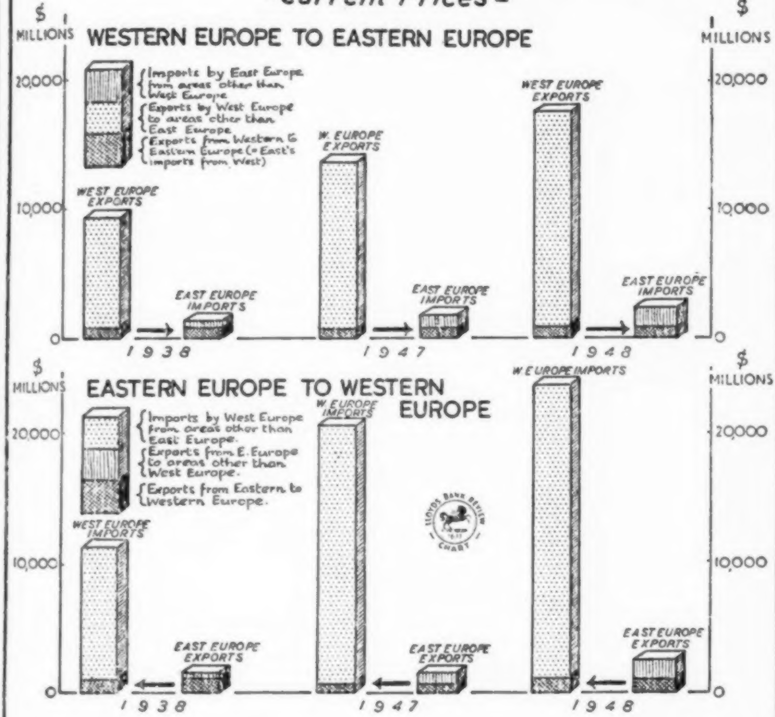

THE TOURIST INDUSTRY
VISITORS TO THE U.K.
THOUSANDS
From British Countries
From other foreign countries
From U.S.A.
0
100
200
300
400
500
1936
1937
1938
1947
1948
1949 Estimate
VISITORS TO U.K. 1948
INCLUDING VISITORS IN TRANSIT
NUMBER: 558,000
FROM STERLING AREA
FROM DOLLAR AREA
FROM OTHER COUNTRIES
EXPENDITURE: £33,000,000
VISITORS FROM DOLLAR AREA
VISITORS FROM STERLING AREA
VISITORS FROM OTHER COUNTRIES
AMERICAN VISITORS TO EUROPE
THOUSANDS
NUMBER OF VISITORS
MILLIONS OF $
EXPENDITURE OF VISITORS
1928/38
1946
1947
1948
SOURCES: Board of Trade Journal
British Tourist & Holidays Board
Third Report to Congress of E.C.A



NOTE Figures include trade of the U.S.S.R.
SOURCE: U.N. Economic Survey of Europe in 1948.

EAST-WEST EUROPEAN TRADE

-Current Prices-



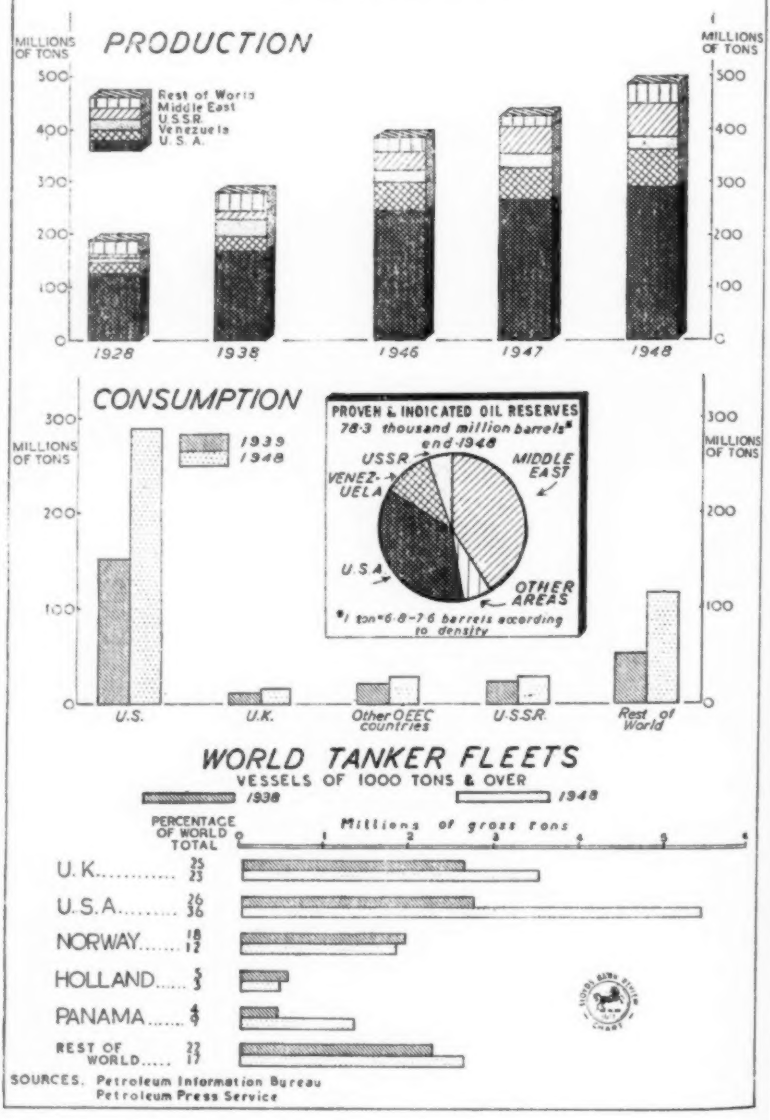
VOLUME OF TRADE
at 1938 prices

	Total West Exports	West to East Trade	Total East Imports	Exports from West to East as percentage of :— Total West Exports	Total East Imports
1938	100·0	100·0	100·0	*7·8*	*58·5*
1947	67·4	40·2	71·3	*4·7*	*32·9*
1948	83·6	43·4	82·6	*4·1*	*30·7*

	Total East Exports	East to West Trade	Total West Imports	Exports from East to West as percentage of :— Total East Exports	Total West Imports
1938	100·0	100·0	100·0	*71·3*	*9·2*
1947	42·6	26·9	82·3	*45·0*	*3·0*
1948	71·0	40·6	86·9	*40·8*	*4·3*

Note : Eastern Europe includes U.S.S.R.
Source : U.N. Economic Survey of Europe in 1948.

PETROLEUM



SOURCES. Petroleum Information Bureau
Petroleum Press Service

BENELUX AND WORLD TRADE

Thousands of millions of U.S. dollars.

	WORLD EXPORTS	Exports of							
		U.S.A.		U.K.		Benelux [1]		Canada	
			%		%		%		%
1938	22·1	3·1	*14·0*	2·6	*11·8*	1·7	*7·7*	0·9	*4·1*
1946	35·0	10·2	*29·2*	3·9	*11·1*	1·2	*3·4*	2·3	*6·6*
1947	50·4	15·4	*30·6*	4·8	*9·5*	2·5	*5·0*	2·9	*5·8*
1948	56·3	12·6	*22·4*	6·6	*11·7*	3·3	*5·9*	3·2	*5·7*

	WORLD IMPORTS	Imports of							
		U.S.A.		U.K.		Benelux [1]		Canada	
			%		%		%		%
1938	24·9	2·2	*8·8*	4·5	*18·1*	1·8	*7·2*	0·8	*3·2*
1946	40·4	5·7	*14·1*	5·3	*13·1*	2·4	*5·9*	2·1	*5·2*
1947	56·0	6·5	*11·6*	7·2	*12·8*	4·1	*7·3*	2·9	*5·2*
1948	63·6	8·1	*12·7*	8·4	*13·2*	4·5	*7·1*	2·9	*4·6*

[1] Figures include Indonesia and Belgian Congo and also Belgo-Dutch Trade.

SOURCE: International Monetary Statistics (I.M.F.); cf. Overseas Economic Surveys "Belgium," 1948, p. 15.

BENELUX: EXTERNAL TRADE

Millions of dollars at current f.o.b. prices.

BELGIUM AND LUXEMBURG

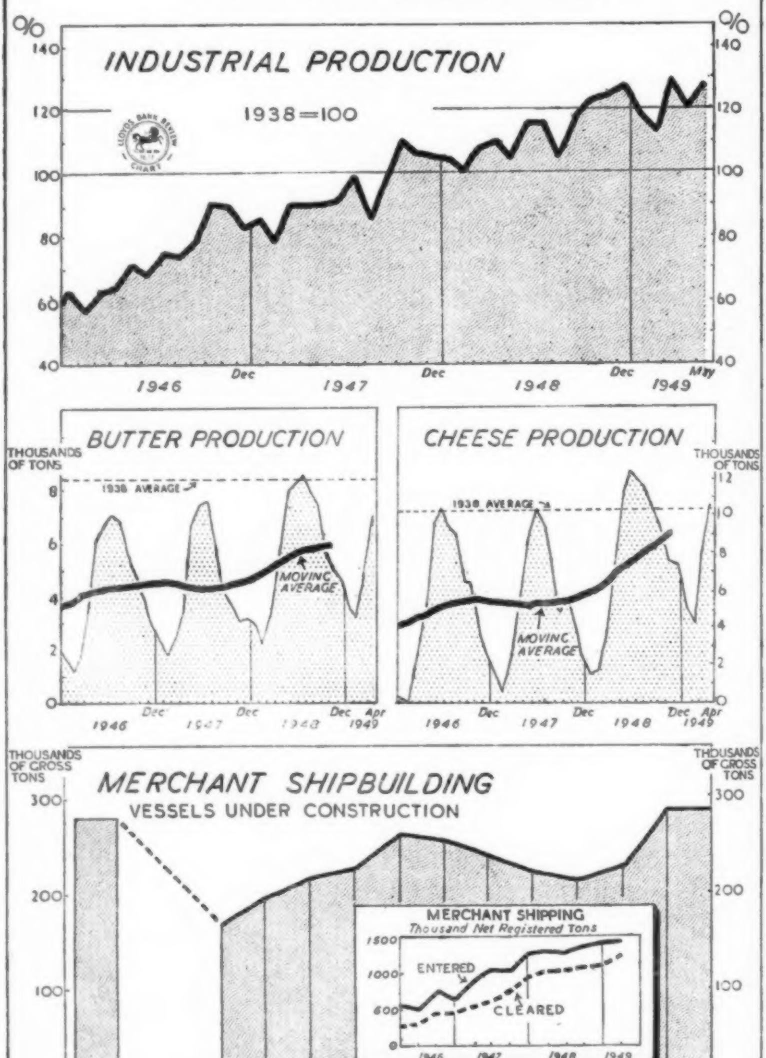
	Imports			Exports		
	Total	From Netherlands	%	Total	To Netherlands	%
1938	702	58	*8·3*	721	88	*12·2*
1947	1,764	111	*6·3*	1,399	179	*12·8*
1948	1,799	163	*9·1*	1,665	267	*16·0*

NETHERLANDS

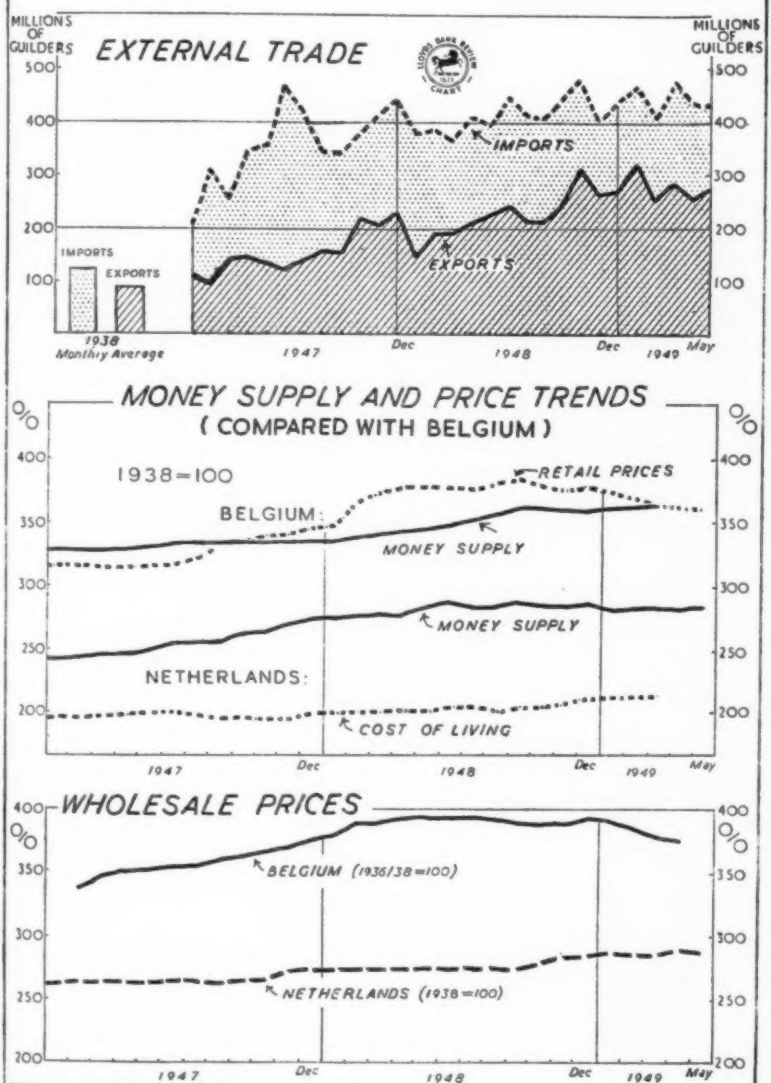
	Imports			Exports		
	Total	From Belgium Luxemburg	%	Total	To Belgium Luxemburg	%
1938	732	88	*12·0*	579	58	*10·0*
1947	1,405	179	*12·7*	711	111	*15·6*
1948	1,728	267	*15·5*	1,025	163	*15·9*

SOURCE: "Economic Survey of Europe in 1948" (United Nations).

THE NETHERLANDS

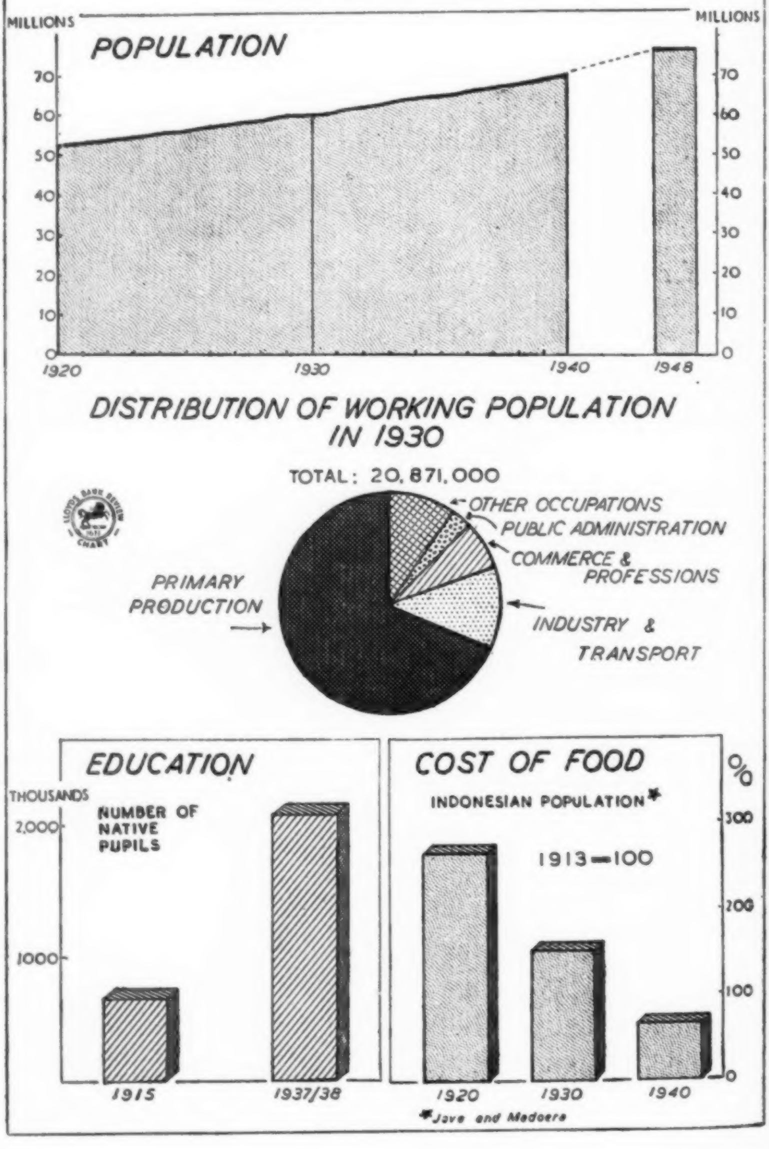


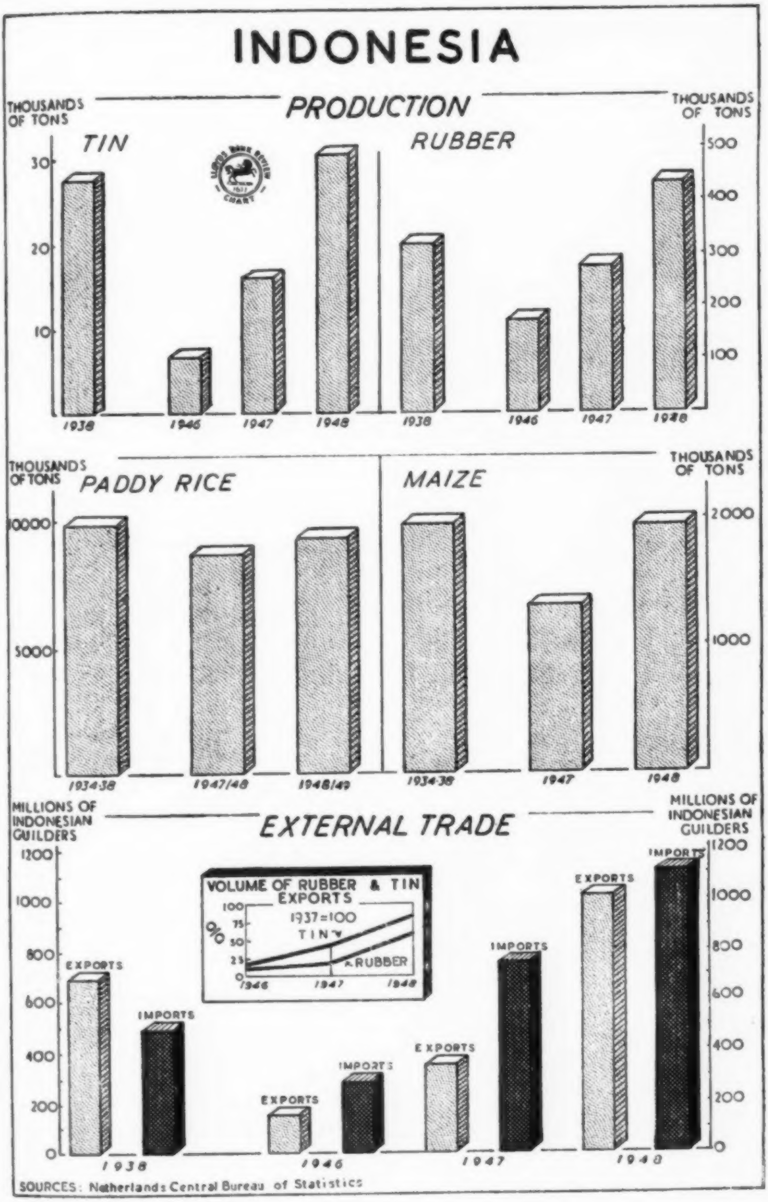
THE NETHERLANDS



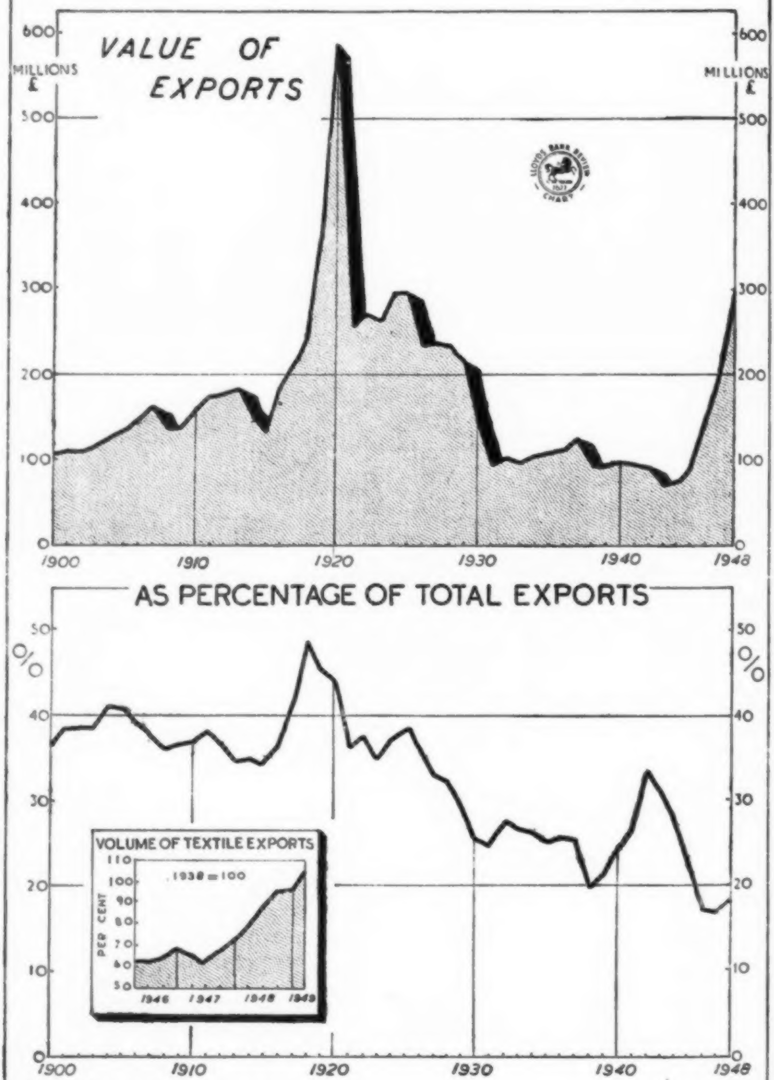
SOURCES: U.N. Bulletin of Statistics
I.M.F. Financial Statistics

INDONESIA


MILLIONS
POPULATION
MILLIONS
70
60
50
40
30
20
10
0
1920
1930
1940
1948
DISTRIBUTION OF WORKING POPULATION IN 1930
TOTAL: 20,871,000
OTHER OCCUPATIONS
PUBLIC ADMINISTRATION
COMMERCE & PROFESSIONS
INDUSTRY & TRANSPORT
PRIMARY PRODUCTION
EDUCATION
THOUSANDS
NUMBER OF NATIVE PUPILS
2,000
1000
1915
1937/38
COST OF FOOD
INDONESIAN POPULATION*
%
1913 = 100
300
200
100
0
1920
1930
1940
*Java and Madoera


INDONESIA
PRODUCTION
THOUSANDS OF TONS
TIN
RUBBER
1938
1946
1947
1948
PADDY RICE
MAIZE
1934-38
1947/48
1948/49
EXTERNAL TRADE
MILLIONS OF INDONESIAN GUILDERS
EXPORTS
IMPORTS
VOLUME OF RUBBER & TIN EXPORTS
1937=100
TIN
RUBBER
%
SOURCES: Netherlands Central Bureau of Statistics

TEXTILE EXPORTS



SOURCES: Board of Trade Journal
Trade & Navigation Accounts.